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OF

ECONOMICS, POLITICS, AND SOCIOLOGY

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INTRODUCTION TO
BUSINESS ORGANIZATION

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INTRODUCTION TO

Business Organization

BY

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PREFACE

This volume is an outgrowth of a course of lectures on Business Organization and Management delivered at the University of Wisconsin in connection with the courses in Commerce. There is no single volume covering modern business activity from the point of view of organization. It is, however, true that occasional articles in trade magazines and even treatises covering special phases of business have recently come from the press.

The growth of this literature indicates a larger interest in the systematic study of business institutions and operations. The business man is fast realizing the practical helpfulness of these studies. The best firms are establishing trade and technical libraries and schools of instruction, not only for the training of their employees, but also for constant consultation in connection with office and factory problems. Greater attention is given to-day to business efficiency, and several reasons have made this necessary, among the more important of which are business waste and misdirection.

Every business man, although he may deny that there is a science of business, will admit that there is a proper way of organizing *his* business.

It is obvious that the best method of discovering this is to study business institutions and processes; but the difficulties of presenting adequately the essential facts of business organization are apparent to those who have given the subject any attention. The paucity of literature upon this phase of business is possibly the greatest difficulty to be encountered. At the same time, this lends a special interest to the subject. It is essentially an untrodden field. The material must be gathered from scattered and unrecorded sources, and the difficulties are therefore great and often almost insurmountable. In fact, the subject cannot be adequately treated before the various lines of business activity are covered monographically. This means a great expenditure of time and effort.

The aim of the present volume is to discuss in an elementary way the important phases of business organization. Its scope precludes any attempt to discuss business management, except in so far as it throws light upon the problems of organization. The details of management must be left for more pretentious efforts, but illustrative material has been freely incorporated so long as it did not involve too much detail. My purpose is to discuss in outline the more important phases of business organization in the hope that a useful service may be rendered. The needs of the student and clerk have been con-

stantly in mind in the preparation of this volume. If I have succeeded in conveying the significance of business problems, and the value of a closer study of them by young men entering upon a business career, I have been fully repaid for the time and effort devoted to the collection and discussion of the widely scattered facts covered in these pages.

The plan of treatment has been somewhat arbitrary. Not having the advantage of any work covering the subject, I was compelled to pave the way. The material naturally suggested its grouping into two broad divisions. The first division is introductory, and is devoted to the classification of business activities, and especially to the legal aspects of business organization. The second division is devoted to a discussion of the principles of organization, the simplest forms of which are illustrated by a chapter on farming, followed by three chapters on the organization of manufacturing, and by several chapters on the organization of distribution. Among the subjects treated here are exchanges, direct selling, wholesaling and retailing, traveling salesmanship, the mail-order business, credits, collections, and advertising. The classification and division of chapters may be open to objection, but they seem to suit the limited scope of this volume.

I desire further to add that there has been a complete adherence to the point of view of the

organizer and manager of business undertakings in the preparation of these pages. The purely social and economic phases have been passed over, except in so far as they threw light upon the problems of organization. At every step the social and economic effects of special forms of organization are apparent, and while these questions are intensely interesting, the lack of space alone would prevent their treatment in these pages, even if they were not excluded for other reasons.

I am indebted to many persons for aid, not only in the collection of material, but also in passing judgment upon the manner of its treatment. When it is understood that these facts have been gathered largely through correspondence and personal consultations with business men, it will doubtless be fully appreciated that any attempt to acknowledge by name the debt incurred would be impossible in a preface. Although personal acknowledgment will be omitted, I desire, however, especially to explain the method employed in the final preparation of each chapter. In order to have a sense of security and ease of mind in the final plan of treatment, I had each chapter critically read by two or three business men whose special knowledge and large experience render their opinions authoritative. This is not urged because the writer desires to escape responsibility for any errors that this book

may contain, but because he believes that it attaches to its pages a value which would be wanting had the subject been treated solely from the academic point of view.

S. E. S.

MADISON, WISCONSIN,
August 1, 1906.

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INTRODUCTION TO BUSINESS ORGANIZATION

PART I

INTRODUCTORY

INTRODUCTORY

I

GENERAL CONSIDERATIONS

A survey of our modern life impresses upon us the value and importance of organization in business, politics, and society. The nature and efficiency of this organization may be taken as a fair index to the progress made in these fields. The business man, as well as the student of economics, must assign to organization a leading position among those forces which have made possible our present industrial era. This is not alone true of the present, but likewise during other well-known periods of industrial activity business organization attained a high degree of development and exerted a far-reaching influence.

In discussing the problems of organization we shall keep before us the point of view of the organizer and manager of business undertakings. Our primary aim shall be to outline our business institutions, as well as to point out the dominant business tendencies of to-day. Science is based upon accumulated experience. Classification is the result of a comparison of differences and similarities. If we cannot do this for business,

it must be because chaos reigns there; but the most casual observation of business life shows us that this is not true. We may describe and classify the facts of business in such a way as to indicate their underlying tendencies and principles. In the conduct of business these principles are consciously or unconsciously utilized. Every business institution is related definitely with those which immediately preceded it, and in the same way business practise is related to the practise which preceded it. Business is an evolution, like government.

The purpose and significance of organization and management in business may be shown by a brief characterization of each. Organization may be defined as the act of bringing together related or interdependent parts into one organic whole. If we apply this general definition to business, it would read as follows: Business organization is the bringing together of the related or interdependent parts of business into one organic whole. We observe that organization is the process of arranging, systematizing, and combining those elements which are related naturally and organically in such a manner as to make them a unit. In this way the constituent elements of insurance, transportation, manufacturing, and distribution are organized into definite business undertakings.

Such a relationship we call a business, a firm,

or a house. For instance, the organization of a factory involves the selection of an administrative and labor force. Departments are created, and over each is placed a superintendent or manager. In a similar way the president of a railway combines those forces which relate to railway transportation. And thus throughout business there is going forward the selection and combination of those elements which are to constitute the organization; and the wisdom and skill exhibited in the selection and adjustment of those elements which naturally combine to form the organization are the recognized indications of ability in business.

The idea of management is readily expressed by the current phrase—business policy. Management properly begins after the organization has been perfected, and is therefore concerned with the development of a business policy. It is the actual conduct of business affairs. The manager has at his disposal various departments, and it is by directing these that the policy of the firm is developed. If business principles have any value, they should be uniform for similar conditions, for business administration consists in the application of well-recognized experience and practise to a specific business problem. The efficiency of management is ultimately measured by the profits of the business.

With this brief characterization of organiza-

tion and management, we may now turn to a consideration of their value in business. Recent years have witnessed the rise of a class of business men whose talents have been devoted to the organization and management of business enterprises. They are called the captains of industry, because upon them falls the responsibility of promoting and organizing industrial undertakings. This organizing talent has created a series of intricate business institutions, and has won for itself a position of influence and power.

The manager of a business must secure the greatest efficiency and economy. In order to attain these, he must be fully acquainted with the elements that combine to form his organization and to shape his business policy. He must be familiar with the labor problem, the work of the various departments, the systems of cost-keeping, the legal aspects of trade—in short, he must be familiar with the technique of his business and its relation to economic conditions.

There is a general impression that business is largely of a routine nature. While it is doubtless true that the work of the holders of subordinate positions in the larger organizations is routine, yet we should not fail to appreciate the fact that the higher positions give opportunities for creative work. It should be the aim of the manager to organize his business so that it will "run itself." When a business is so organized,

the manager is then able to devote his time to larger affairs, leaving the details to be worked out by competent department managers. In other words, a properly organized business demands two kinds of talent: one class of workers must perform the clerical work, while a more select group is devising and initiating new methods and policies. In this way the application of correct principles of organization is utilized, and a high degree of efficiency secured. This is amply illustrated by a study of the methods of well-known business houses. Efficient organization is vital to their continued prosperity. On the other hand it is well known that imperfect organization has often threatened their existence, and the failure to adjust the organization to changed business conditions has resulted disastrously in many instances.

It is generally asserted that the superiority of American firms over British is due to the more efficient organization of the former. Again, it is urged that the success of German houses in competing with English, and even American, firms is due, not only to the attention which they give to the technical phases of business, such as engineering, chemistry, etc., but also to a more thorough study of business organization and methods. Everywhere progressive firms are ready to utilize new methods, and to change their organization when it can be shown that such

changes will yield better results. The more complex business conditions become, the higher the degree of skill required in directing the organization and management. A great business has been compared to a military organization, where all the parts are carefully grouped and officered. Each division is assigned to a particular work and discipline is carefully maintained.

We are accustomed to speak of business in its public and private aspects. We speak of the work of government as the administration of public business, while, on the other hand, we refer to the management of a firm as the administration of private business. While these two are quite distinct in their purposes, they do, however, present many points of similarity in organization and methods. The object of public administration is to promote social well-being. It is not performing its work for financial profit, but rather to improve social conditions. In order to accomplish this end, taxes must be levied and expenditures made for public improvements, education, police, and other purposes. The successful prosecution of this work requires correct business methods.

The object of private administration, on the other hand, is, primarily, to secure present and prospective financial profit, and the success of the business is determined ultimately by this standard. While many private business under-

takings are quasi-public in their character, such as lighting plants, water-works, and street railways, still, so long as they are privately managed, financial gain will be the controlling motive. Obviously, in many fields of administrative activity it is difficult to draw the line sharply between private and public business. In many instances the line can only be drawn vaguely, and then only by keeping before us the thought that public business has in view primarily social advantage, while private business has as its primary purpose financial advantage.

Business undertakings grow out of general economic conditions. In a primitive society we find only a few traces of definite business undertakings. Each person provides for himself in his own way. The producer is virtually the consumer, and where the exchange of commodities takes place it is in the form of the simplest barter. In the more advanced stage of economic society wants become more varied—a fact which gradually leads to a specialization of effort and to the appearance of definite business institutions. The producer and consumer are more widely separated; hence, to accomplish the exchange of commodities, business organization becomes necessary. By way of illustration the grain business may be cited. The concentration of population in certain parts of the world, far removed from the grain surplus producing areas, has necessi-

tated the development of systems of transportation, the establishment of mills, the organization of elevator companies and commission firms, in order to move the surplus grain and flour to the distant consumer. In the same manner the cotton, tobacco, or coal business is developed to bring these commodities from the producer to the consumer.

During periods of great industrial activity we find that the organization of business becomes more complicated. Before the development of the Roman law, we find few traces of the characteristics of business organization. We know something of the wealth and power of the merchant princes of the ancient cities, but we know little of the business methods they employed.

The Roman legal system gives us some idea of the nature of the business institutions of that day. It developed some of the essential features of partnership. But the business of the Roman was largely of a local character. With the German invasion the Roman commercial organization was virtually destroyed and the machinery of business swept away. In the eleventh century, however, commerce began to revive, and gradually manufacturing industries grew up in the cities, and mercantile institutions were established. Fairs were held in France and Germany and, in fact, throughout all Europe. These markets were the meeting-places of merchants,

who often came great distances to attend them. The merchant princes of north Europe sent their ships to distant ports, and trade caravans crossed the country from market to market. By the fifteenth century the business structure became more complex and the area of commerce was extended.

The cities were the centers of manufacture and trade, and gradually grew in wealth and power. As a result of this widespread economic activity a type of industrial organization was developed which was virtually universal for the period. Producers and merchants organized themselves into groups or gilds for the manufacture and sale of particular wares. These gilds dominated the commercial life of that time. They framed the rules and regulations governing manufacturing and marketing. Under the gild system commerce greatly prospered, and the names of the merchant princes of that day are almost as familiar as those of its kings and rulers.

The age of discovery opened up new business possibilities and extended the commerce of Europe, thus calling for a readjustment of the commercial organization. Larger capital was required, and new investments were made in distant business ventures. All these involved greater risks, and, in order to minimize them, better legal protection became necessary. The need of some more elastic organization was fully

recognized. New forms of investment required the capitalist to put his money into ventures where it was impossible for him to give the business his personal attention, and he was compelled to rely upon the honesty and business judgment of his managers. The partnership rendered his liabilities great, and any mismanagement might sweep away his private fortune. In order to limit the risks of investment where it was impossible for the investor to give to the business his personal attention, the corporation was gradually developed.

The corporation at first took the form of a joint-stock company, and was employed mainly to carry on business ventures in newly discovered countries. While the Romans had suggested the corporation, the commercial instinct of the Anglo-Saxon gave it the position of usefulness in commerce which it now holds. The discovery of new lands which fired the commercial spirit of Europe led to the organization of the great trade companies of England and Holland. They were organized essentially as corporations, and are still familiar figures in the trade and commerce of to-day. The East India Company and Hudson Bay Company go back for more than two centuries for their beginnings. In 1692 at least three of these companies existed in England, and similar corporations still exist. They were not only regarded as corporations for private business pur-

poses, but were also employed for the administration of public affairs within the territory granted to them by the Government.

At the end of the seventeenth century the advantages of a corporation for business purposes were fully realized, and charters for the conduct of various kinds of business ventures were frequently sought. In 1720 about two hundred corporations existed in England alone. Blackstone in 1776 cited banking, insurance, public improvement, and municipal water-supplies as the legitimate fields of corporate activity. At the end of the eighteenth century this field was greatly extended, and as a result corporation law was more highly developed.

In the early part of the nineteenth century the full significance of corporate activity comes upon us with the rapid growth of industrialism which followed the utilization of coal and iron, the invention of the steam engine, and the development of electric power. We find that the older business methods and types of organization, such as the individual and partnership, were wholly unable to cope with the new business problems, and consequently were rapidly displaced by the corporation in all lines of business activity which involved great risks of investment and management. Thus, starting with the individual merchant, business activity has evolved the part-

nership and corporation to meet the increasing complexity of industrial processes.

The relation which business organization sustains to general economic society may be further illustrated by classifying the various business units in accordance with the accepted classification of economic science. Business organizations may be variously classified, but, by following the suggestion of the economist, we may divide them into the following divisions: 1, extractive; 2, manufacturing; 3, commercial; 4, transportation. The three classes most generally recognized are the extractive, manufacturing, and commercial or distributive activities. While these three groups correspond to the broad divisions of economic science, specialization within each field necessarily implies the existence of many separate business units which serve as connecting links.

An examination of the extractive business activities reveals a field divided into innumerable separate simple organizations. An extractive business is one in which raw materials of commerce are produced for the purposes of consumption or manufacture. The extractive business is confined to production. Its most important phases are agriculture, mining, and forestry. Agriculture relates to the cultivation of the soil. In its general aspect it comprises such special kinds of farming as wheat, fruit,

cotton, tobacco, dairy, poultry, etc. These constitute the most important divisions of agriculture, and are indeed among the most important of our business life. The second division of the extractive field is mining. The function of mining is to bring to the surface the mineral deposits in order to utilize them in the arts and in commerce. The well-known mining operations are coal, copper, gold, silver, tin, zinc, and lead. The third division of the extractive group is forestry. In its broad sense its function is to make available the forest products, and upon it are built such manufacturing activities as lumbering, rubber, paper, and furniture.

An analysis of these various special undertakings shows that each has peculiar limitations. They are essentially local, and are controlled in a particular way by soil and climate. If we take tobacco as an illustration, we find that its commercial value depends intimately upon soil and climate. Mining is peculiarly local. It will also be observed that these industries are subdivided into innumerable small undertakings. For instance, general farming is carried on as innumerable separate enterprises. The difficulty of operating over a large territory compels this extreme subdivision. It will also be observed further that many of these activities are governed by the seasons of the year. In farming and lumbering we find intense activity in certain

seasons, while in other periods almost none. They contrast sharply with the factory system, which goes on with uniform activity throughout the whole year. Again, viewed as separate business organizations, this type is comparatively simple in structure, but on the whole these enterprises represent in the aggregate great capitalization, organized and conducted as separate undertakings.

The second division of our general classification includes manufacturing. Manufacturing adds new value to a commodity by changing its form, and this new value is added mainly through the additions of labor, capital, and cost of management. A manufacturing plant is therefore an organization both technical and administrative, whose function it is to give to a product new value by changing its form. Manufacturing ends with the completion of the factory processes, and theoretically it has nothing to do with the purchase of the raw materials for the factory or with the distribution of the finished output. Of course, factory managements do buy their raw materials, and distribute their finished products, but in so far as they take up this work they engage in commercial activity in addition to their manufacturing business. It will be found that the line between the factory and the commercial phase of manufacturing is not so sharply drawn in practise. Among the more important

lines of manufacturing are farm implements, machinery, steel, hardware, dry-goods, refineries, packing-houses, tanneries, furniture, and chemicals. Manufacturing is characterized by great specialization. Furthermore, the factory operates throughout the year without any necessary interruptions, unless it is for business reasons. Scarcely any other business is so little influenced by nature. Consequently the capital invested may be constantly employed, while in many other business lines in certain seasons investments are relatively unproductive. However, in some lines of manufacturing the demand is dependent upon the seasons of the year, and this compels often the storing of large quantities for future distribution.

There remains a third class of business undertakings which is generally designated as commercial or distributive. It includes a wide and varied activity. For convenience, we may divide these activities into two general groups, marketing proper, and those undertakings which facilitate exchange, such as banking and credit institutions. By marketing, we refer to those commercial processes which are concerned with the distribution of the raw materials of production and the finished output of the factory. These business interests are engaged in distributing the various commodities among the consuming classes. Their function is to give additional value

to these commodities through exchange. The particular function of distribution is to organize the market, and to establish a meeting-place for the seller and the consumer. In the field of distribution we find a vast variety of undertakings. These are based mainly upon agriculture, mining, and manufacturing. Among the more important raw materials to be distributed are cereals, cotton, produce, live stock, iron, coal, and petroleum. The distribution of the output of the factory includes dry-goods, hardware, machinery, woolen and cotton cloth, boots and shoes, and a great variety of other lines.

The organization of the distributive machinery will naturally be determined by the relationship existing between the producer of raw materials and the manufacturer and the consumer. If the commodity passes directly to the consumer through retail stores, as is often the case in the local market, the distributing processes are correspondingly simplified. But if, on the other hand, the raw materials or manufactured wares are sent to distant markets, greater capital and a more elaborate organization are required.

The second phase of commercial activity includes banking and credit institutions. These comprise banking and loan firms and those agencies gathering commercial information and extending protection, such as bonding and insurance companies. Their function is to provide

a safe depository for capital, to secure loans, and to assist in various ways in the work of distribution. A cotton merchant takes a consignment of cotton in some distant market, draws his draft upon his bank, which in turn undertakes to complete the transaction. In case credit is requested the dealer may use such agencies as Dun and Bradstreet to acquaint himself with the financial standing of the merchant. These commercial institutions provide banking facilities, extend financial assistance, and give credit information and assume in many other ways financial and commercial responsibilities.

Finally, the fourth class of business undertakings is transportation. The function of transportation is to move the goods of commerce from place to place, and it should not be concerned with its marketing. It gives new value to the commodity by changing its place. It takes the surplus of the cereal belt and transports it to the markets of the East, and takes the product of the factory to the consumer. Among these are such familiar activities as railways, both general and urban, drayage and transfer, steamship and canal transportation. These great organizations have grown up mainly because of the needs of distribution, and offer a wide and interesting field for the study of business organization.

These four main divisions, with their special groups, include the essential business activities of

to-day. Other classifications might be made, but the one given will be generally recognized as corresponding in all essentials to present business practise. Through this classification we are able to observe how our ordinary business activities concretely embody the underlying principles of production, manufacture, and distribution. It places business upon a scientific basis.

II

ELEMENTS OF ORGANIZATION

We have previously noted that the organization of business is the selection and arrangement of those elements which naturally combine to produce a business establishment or firm. Many of these elements are of a general character, and it is by their selection and combination that specific organizations are created. It is therefore desirable that the business man be familiar with these general characteristics of business organization.

One of the first problems of organization is the selection of the administrative and labor forces. Where large bodies of men are to be brought together, their selection becomes an important and often a very difficult problem, but it is impossible to lay down hard and fast rules governing the choice of men for the office and labor forces. In fact, the selection of employees is one of the best tests of the ability and judgment of the manager, for it indicates a quality of mind which is characteristic of successful business men.

In making the selection of his administrative and labor forces, the manager has in view certain personal traits and qualities which are considered

everywhere as the basis of business success. The most important of these are the physical, intellectual, and moral qualities of the applicant. Naturally, the emphasis upon these qualifications will vary with the position; but, in a general way, it is obvious that a man of strong and vigorous physical powers will accomplish more in a given time than one who is not so endowed, and likewise an alert mind will be more efficient than a slow and sluggish one. Again, it is very generally recognized that good moral habits are desirable in business, especially where great responsibilities must be assumed. For this reason immoral habits absolutely debar one from positions of trust and responsibility with the best firms. In more recent years some of the great railway systems have enforced strict orders against cigarette smoking and drinking on the part of their employees when on or off duty. Gambling on the part of the employee is not tolerated by business firms. On the other hand, regular habits of life are encouraged, and many commercial houses even keep watch over the companionship of their employees and the manner in which they spend their leisure time.

The importance of these simple considerations is apparent when we measure their value in the light of business efficiency. Everything that tends to promote efficiency is vital. The efficiency of any body of men goes back essentially

to the physical, intellectual, and moral capacities of each individual. A great railway system or manufacturing plant is efficient or weak in proportion as these qualities have been regarded in the selection of the labor and administrative forces.

The careful policy pursued by the best firms in selecting their employees is fully demonstrated by the character of the questions asked those seeking employment. Of course, the nature of the inquiry depends upon the character of the business, and of the position, but even in the lower ranks searching questions must be satisfactorily answered. Obviously the more highly developed the organization is, the more careful must be the attention given to this side of the problem. A manufacturer must give greater attention to the selection of his force than the managers of the more simple business organization.

The primary purpose in guarding the selection of employees is to harmonize talent and fitness with the employment or the position. The value of these considerations is still further emphasized by the policy pursued by many business houses in providing many things for the convenience and pleasure of their employees, for the reason that in the end it will make them more content, and consequently more efficient. Where the welfare of the employee has been disregarded, legislation often compels the firm to maintain a wholesome

physical and moral environment, and while this policy is pursued on the ground of public policy, it indicates in a general way the value of these qualities in promoting business efficiency. These regulations generally relate to the ventilation of factories and offices, the labor day, and the employment of women and children. The best business houses recognize that a wholesome environment both in and outside of business is of primary importance.

The problem before the manager, therefore, in the selection of his clerks and employees is to find those men who will work together under one supervision without friction and waste. A general rule of great value is that specialization shall be carried out so that the employees shall not divide and dissipate their energies. The division of labor is an economic and administrative necessity. Accountability must be clearly and accurately defined. The energy and efficiency of the force must be sustained, and the personal interest of the employers kept foremost in the minds of the employees. Responsibility in private administration is as essential as in public administration. The clerk must turn out accurate work with the same precision that the factory employee turns out a piece of machinery. This skill and precision are secured by applying the principle of the division of labor to business, so that each clerk or laborer is confined to those

operations which require the exercise of special talents and skill.

A recent report of Bradstreet relating to business failure throws some light upon the qualities necessary to business success. The statistics show that a large percentage of the failures may be traced to poor business judgment, and not alone to the lack of capital. A lack of capital has brought about one failure in three, incompetency one in five, while extravagance and speculation each one in one hundred. These ratios indicate the value of a high standard of judgment in business practise. These failures must be charged in the main against business managers, and not against the working force, and they indicate the value of a thorough knowledge of business elements as a preparation for success.

It is obvious that complete obedience in the performance of duties is required of all employees. The individual must subordinate his own personal desires to the rules and regulations of the firm. In short, anything that will destroy the *esprit de corps* of the clerical and labor forces will bring disaster to the business. Insubordination endangers efficiency. The interests of the business are paramount, and all the efforts of the force must be so concentrated and utilized as to produce the largest efficiency. Private interests must be forgotten and indifference weeded out. The management is always alert in recognizing

individuality and personal efficiency in the ranks of the service. The work of the employees is carefully studied and observed, and systematic and orderly habits are always rewarded.

In summarizing these considerations, too much stress cannot be placed upon a wise and careful selection of the administrative and labor forces. The physical, intellectual, and moral qualities of the men are paramount. These combinations produce strength and efficiency, and, combined with executive ability and judgment, we have the foundations of a successful business organization. Such a force will prove strong at all times, and will be resourceful in the development of methods and effective in their execution.

There are other elements relating to business organization which must be considered. In the interests of economy and efficiency, great improvement has been made in recent years in office aids and facilities. It has been amply shown that the office is capable of handling a larger volume of work by equipping it with those aids and appliances which will relieve the force, in so far as possible, from the care of details. This is good business practise where it can be done more systematically and accurately by the use of improved records and devices.

In the first place, more attention is given to-day to the arrangement of office space, and particularly in dividing it so that the business processes

go on naturally and logically. Much greater attention is now given to the selection of office furniture and equipment for the records of the business. It is quite obvious that these aids and appliances will differ with the business. The attention given to this side of the office organization has resulted in larger efficiency and has greatly reduced the expenses of management.

No better illustration of this new movement in business is found than in the recent development of the card system as applied to office organization. In every well-organized office of to-day this system is employed in keeping the records, and is utilized in every department of business. This development has been phenomenal during the last few years. Another appliance which is very widely used to-day is the cash register, which minimizes the work of the bookkeeper, and provides an excellent check upon the clerks. Again, the use of tubes and trolleys in the large department and retail stores for the delivery of goods and cash affords another excellent illustration of the value of mechanical aids in the organization of the business. This remarkable development has greatly influenced the character of business organization in very recent years. It has greatly aided in the efficiency of the organization as well as resulting in much greater economy. Wherever mechanical devices and aids can be used greater accuracy and economy

will result. It enables the manager of the business to keep closer watch over the details and gives a more accurate control over the operations of his organization.

It is a well-recognized fact that the division of effort and centralization have gone on rapidly in the business world. The growth of large firms has made necessary the organization of departments in order to exercise control over all the parts of the business. Consequently the extent to which the principle of the division of labor can be applied to any given business will determine the efficiency of the organization. The differentiation of functions within the business organization indicates a high degree of development, provided that unity and harmony, economy and energy, are not sacrificed. This principle of special effort, combined with central supervision and control, is of far-reaching importance in business. The principle may be violated by too much or too little specialization, and it is the duty of the manager to separate his business processes and to constitute them into separate departments. He must group those operations of a similar kind into one department.

We have briefly summarized some of the more important elements in order that their value as the general groundwork of the business structure might be suggested. It is out of these simple elements that every business organization is

constituted. They are of universal application throughout the business world. They combine to produce the simplest business unit, or apply to those organizations involving the harmonious action of thousands of men which reach out over the continent and even across the seas. They are in themselves so simple and universal that at times the business manager may fail to realize their far-reaching importance. But it is upon the clear and careful application of these principles that the efficiency and success of business is dependent.

III

LEGAL ASPECTS OF BUSINESS ORGANIZATION

With these introductory considerations before us, we may pass to an examination of the legal aspects of business organization. It is quite obvious that it is necessary to fix legal responsibility in our daily business operations. As a result, commercial law has rapidly expanded in recent years. Business institutions and methods have been given a legal setting for the purpose of fixing responsibility in all of its phases. In a simple business community the legal rules are likewise simple, but with business growth and expansion comes a corresponding growth of the law governing such transactions. The managers of large firms and establishments must be made responsible in their work. Again, the investor must have protection or he will not put his capital into business ventures. As a result, the law furnishes the foundation for all business transactions. It is our purpose to point out briefly how this has been brought about, and especially how the law has influenced the organization of business.

From a legal point of view business organization may be divided into two classes—non-

corporate and corporate. In the first type the individual assumes legal responsibility, and in the second this responsibility attaches to an artificial legal entity or person—the corporation—but not to the individuals that control the corporation. There are certain intermediate steps between these two types, but they may be considered as modifications of the one or the other. For instance, the partnership is a combination of individuals, but still the liability of the individual partner and of his private property for the debts of the partnership are essential features of this type of organization. On the other hand, we have to-day a class of artificial legal entities made up of several corporations, but in which the identity of the component corporations is generally maintained.

The purest example of the first class is the independent business man. Its leading feature is the full responsibility of the individual. He assumes all of the risks connected with investment and management, and, except in rare instances, this results in a simple business structure. Its activity is confined to local business, and scarcely ever reaches beyond a given community.

The reason for this limited position of the independent business man in our modern complex commercial system is quite obvious. In the first place, there is the limitation of capital, for to-day the amount of capital necessary for successful

business operations grows rapidly as the field expands. Consequently the necessity for a larger investment, in order to organize and conduct a successful business on a large scale, compels the business man to seek relief by uniting his capital with that of others. This also implies the union of responsibility in management.

In the second place, we find that the limitations upon management are even more exacting. The person who alone invests his money in a business undertaking must give to it his constant care and attention. He is not only the investor, but also the organizer and manager of the business. In him there is a union of investment and management. In many cases it is impossible for him to give the necessary time and attention to the details of his business. The difficulties of management are often too great, and especially when the fatal mistakes of other partners involve all of his property whether invested in the business or not. In the eyes of the law he must assume a personal liability, which not only follows his investment in the business, but also his entire property in whatever form it exists. This personal liability is one of the serious handicaps to this form of organization. All the mistakes of management fall upon the owner of the business, and all contracts made by employees become a part of his personal liabilities and risks.

It is therefore apparent that the limitations

upon this form of organization are exceedingly great in this day of large and complex business undertakings. It is generally restricted to the smaller business undertakings in the more simple business communities. The individual type is found frequently in certain phases of our modern business system. It is found quite generally in the management of farms, and in the retail business, such as grocery, clothing, tobacco, and similar stores, where a limited capital, combined with a simple organization and personal supervision, can be successfully employed.

The development of the partnership has, however, made it possible to expand the simple operations of the individual so as to enable two or more persons to combine their capital and skill for business purposes. The purpose of this union is to enable a wider business activity and still maintain essentially the same financial responsibility, as if each of the partners were engaged in an independent business.

A partnership is a contract relationship existing between two or more persons who have combined their property, labor, and skill of management for the purpose of joint profit. The essential difference between the individual business man and the partnership lies in the fact that the latter makes possible the combination of capital and management for the purpose of enabling the partners to extend their operations and

to assume additional business risks. A partnership may be composed of persons or corporations, but generally it is composed of individuals. The commercial and legal conceptions of a partnership are often at variance. Commercially, a partnership is viewed as a body distinct from the partners, having rights and obligations of its own. In business the partners are either debtors or creditors of the firm. This is obviously not the legal notion. But the tendency is, however, to merge the two conceptions.

In order to get before us a clearer notion of the function of the partnership in business, a brief examination of the different kinds of partnerships, as well as the kinds of partners, will be necessary. In the first place, we have the ordinary partnership, which generally falls into these divisions: 1st, a particular or special partnership is one created for a single business transaction; 2d, the general partnership is one created for the conduct of some general line of business or kinds of business; 3d, the universal partnership is one in which all the property and services of the parties are united and all profits are for their joint benefit.

The desire to limit risks has resulted in the limited partnership, which is the creation of more recent legislation, and has some of the characteristics of a corporation in that the liability of one or more of the partners is, by compliance

with certain statutory provisions, limited to the amount of their contribution to the joint undertaking. The joint stock company is an example. It is an association of individuals having a given capital, divided into shares, which are transferable without the consent of the other partners. It possesses, however, no seal, and transacts its business as a partnership. It is simply a partnership with transferable shares, and there is no personal liability on the part of the partners. It is a more recent evolution of the partnership, and has in view a limitation upon the risks of the partners, and also enables the individual to dispose of his interest in the business without involving the existence of the partnership or compelling the reorganization of the business when a partner leaves the firm. The limited partnership and the joint stock company are of statutory origin, and are transitional forms of organization lying between the partnership and the corporation.

The nature of a partnership will be more fully understood when some of the characteristics of the partners are noted. The law distinguishes between the different kinds of partners mainly on the basis of their liability. The classes of partners are not necessarily mutually exclusive, nor are the distinctions between them drawn in the law texts of much importance for our purpose except in the case of general and special partners.

All the members of an ordinary partnership are general partners. On the other hand, all the members of a limited partnership are not special partners. One or more general partners must always be present. In some of the States the statutes have limited the liabilities of some members of the firm, who are, under these circumstances, termed special partners.

It will thus be seen that while the essential characteristics of a partnership lie at the basis of all these distinctions, the law has nevertheless recognized varying degrees of liability for the partners. The degree of liability is determined generally by distinguishing between investment and management. While the partnership implies the identity of investment and management, still, the law has tended to relieve in many instances the partner who is merely an investor and has little or no connection with the management. But these limitations form the exception rather than the rule in business practise.

When a partnership is organized, it assumes a firm name under which it does its business. In the eyes of the public the firm name occupies about the same position as a corporate name, but not so before the law. The law goes back of the partnership, and holds the individual responsible for the conduct of the business and for the obligations created. In the public mind the partnership possesses an entity of its own, and a change

of partners may not destroy the business value of the partnership. But legally the situation is different since the new partnership is a new legal relationship established by the combination of different units of capital and skill of management.

A partnership is therefore established by a definite contractual relationship between the parties composing it whereby they assume a firm name and merge their capital and skill for the conduct of a given line of business. A firm name becomes a symbol of the business, but has no legal independence of the members of the partnership; but the general rule is that when a firm name is adopted, the use of another name in the business is not permissible.

The objects and purposes of the partnership are set forth in the articles of agreement. The nature of these articles will, of course, be determined by the nature of the business. It takes the form of a contract. Each person agrees to invest a certain amount of capital in the business and to give a certain amount of time and attention to it without compensation, unless there is a specific exemption of time or provision for extra compensation. Provision is made for the distribution of profits, and the other details are worked out in order to determine the exact relationship which the persons are to sustain to each other. The capital of the firm cannot be put to individual uses. It cannot be withdrawn without

due notice unless otherwise provided in the articles of agreement.

Unless otherwise restricted, the powers of a partner are determined by the nature of the business. When doing any act necessary for carrying on the firm's business in the ordinary way, either partner can make contracts which bind the other members of the partnership. And if these powers are not to be extended to each partner, the articles of agreement should so specify. Each partner is the general agent of the firm in the conduct of its usual and ordinary business. Every business transaction binds all the partners alike unless restricted by the articles of agreement.

The powers of a partnership are usually of two kinds: first, those powers derived from the articles of agreement, supplemented by the nature of the business; and, second, those derived from the nature of the business, although not specified in the articles. For this reason the scope of the business transactions of a partnership become important, and is essential in determining the authority of any one partner to take any action that will obligate his associates.

Every business possesses certain characteristics which materially modify the liabilities of the partners. Usually the power of borrowing money and extending credit is restricted to the controlling partners. The liabilities incurred from

borrowing money are somewhat different from those made by buying upon credit. In buying supplies or stock, the partners may act independently. This is an implied authority, which is derived from the fact that the business must go on, and in order to make this possible, the partners are given considerable latitude in the purchase of supplies and stock.

Partnerships are usually dissolved by death, retirement, or the addition of partners. If the business is to continue, it is done by the new partners. It does not matter how frequently these changes occur to break the continuity of the business; from a legal point of view new liabilities are created with each change, unless some acceptable form of partnership is employed where a transfer of property may take place without the consent of the partners. Usually each change of partners results in the "winding up" of the business. This calls for an inventory of the assets and liabilities accumulated during the partnership. A dissolution may occur at any time, and is usually done by giving notice to the other partners and to the public.

The dissolution of a partnership calls into question an important consideration affecting all business undertakings, but which is especially associated with the partnership type of organization. This is known in business and in the law as "good will." The partnership, by safe and care-

ful management, may have acquired a standing in the community which the public has associated with the firm's name, but which is also associated with the personality of each partner. In the public mind the conduct of the business is closely identified with the partners who have organized and managed the business. Consequently upon the dissolution of a partnership the question as to the right of the partners to engage in business of a similar character in the same community is usually involved. Customers have been in the habit of going to the place of business and often bargaining in person with the members of the firm. From the point of view of business organization this becomes important since the honesty and fair dealings of the partners are taken as a basis for determining "good will." There seems to be some uncertainty as to whether this quality attaches to the partners or place of business. The general practice, however, is for the retiring partner to agree not to start up a business of a similar character in the same place for a specific period of time, generally for one year.

Having before us some of the general characteristics of the partnership, we must now note its place in the business world as a form of organization. We have already seen that the partner is the basis of the organization. This is brought about by the manner in which liabilities are fixed and determined. When compared, however, with

the single business man, the partnership opens up a wider sphere of activity. It enables a combination of capital, labor and skill of management in the exploitation of a larger business field. It occupies an intermediate position between the independent business man and the corporation, especially in the case of the joint stock company. The need of transacting business upon a larger scale than is possible by investment and management under the control of a single individual has led to the perfection of the partnership.

On the other hand, the limitations of the partnership for business purposes are quite severe, except in its special forms. The liabilities and risks go back of the property invested in the business. The property of a partnership is not alone involved, but, in case this does not satisfy the liabilities of the firm, the property of each partner, in whatever form it may be invested, also becomes involved. Thus the partnership liability is similar to that of the individual who independently operates a business and who assumes all personal risks, and hence the selection of a partner is of extreme importance in this kind of an organization. Men do not risk their property when they have any suspicion that their partners are dishonest or are not conservative and successful business men. And while the partnership widens the scope of business activity, it must necessarily occupy a limited place in business by reason of

the severe restrictions placed upon it by the law.

A survey of the business of any community will show that the partnership occupies a half-way place between that of the independent business man and the corporation, both in the scope of the business and in the capital invested. Like the independent business, it is essentially local in its character, and is found more frequently in the smaller cities and in the retail business. It is employed where personal attention can be given to the management, and is based especially upon individual confidence and integrity, and for that reason becomes a useful form of organization within proper limits. The partnership organization is based upon a close relationship between the investment, liabilities, and management, and where the investor cannot give his personal attention to the business it becomes a dangerous form of organization.

We now come to an entirely different type of organization perfected by the law, in which the investments are more widely separated from the management. In order to enable the investor to put his capital into a business without giving to it his personal attention or necessarily participating directly in its management, there has been gradually developed the conception of the corporation. The essential difference between the corporation and partnership lies in the fact that the former exists as a legal or artificial personality, standing

above and distinct from the individual stockholder or member, while the latter does not shield the property of the partners. It is this feature which especially distinguishes a corporation from a partnership, and it is in this characteristic that we find the chief advantage of the corporation over the partnership. A partnership is the result of a contract relationship, while a corporation is the result of legislative authority.

We have found that the non-corporate type of business organization, whether it exists in the form of an individual undertaking or a partnership, is clumsy, dangerous, and inadequate for the needs of business on a large scale. We have seen that through it business failure may bring ruin and disaster upon all of its members, because of the nature of the liability, which searches out the private property of each partner. It is because of this danger that the partnership is displaced by the corporate form of organization where large interests are involved. Corporations usually grow out of previous partnerships, either by conversion or by their consolidation.

The corporation, in its advanced form, is of recent development. It was recognized in a limited way by the Roman law, and later on the Continent, but the English-speaking people, through their commercial enterprises, have developed it into a useful organization for the conduct of business on a large scale. We have

already noted the rise of several important trade companies in the early period of English commerce. Larger attention was given to the legal aspects of the corporation in order to adapt it to the growing needs of industry. The investment of capital on a large scale, where personal attention could not be given to the management, gradually became the dominant feature of industry and commerce.

At the time of the Declaration of Independence probably not more than a dozen corporations existed in the United States; but, with the opening of the West, which called for the construction of roads and canals, and invited other industrial activities, the usefulness of the corporate form of organization became apparent. State legislatures speedily enacted laws governing their organization, and charters were issued in great numbers. It will thus be seen that the corporation is virtually a product of modern jurisprudence, and we must go to the statutes and decisions of the courts for any definite idea of its nature.

The corporation may be characterized as an artificial person having a distinct organization. It has an interest distinct from the stockholder. Probably the most noted characterization of a corporation is given by Judge Marshall in the Dartmouth College case. He says that "a corporation is an artificial being, invisible, intangible, and existing only in contemplation of law."

A corporation is a legal personality. It is capable of being sued, and likewise can bring suits against other natural or artificial persons.

In American jurisprudence it can be created only by the legislature through special or general enactments. Formerly in England, and even in the Colonial period in the United States, the charter was granted by the king, but later this power was transferred to the legislative branch of government. At first it was customary for the legislature to grant a special charter to each particular group of incorporators. But gradually the corporation began to acquire certain fixed characteristics, and finally it became the practise to pass general incorporation laws. So that at present some officer of the State is directed to issue the charter in conformity to the general corporate laws upon the application of the incorporators.

The instrument by which a corporation is created is known as a charter, or articles of incorporation. The number of persons necessary to secure these articles varies in the different States. Usually at least three incorporators are required. The incorporators are required to present certain information relative to the character of the business and the amount of capital to go into it, and upon the presentation of this form, properly certified to the State authority, accompanied by the required fee, a charter of incorporation is issued

to them. The most important requirements are that a certain per cent. of the stock must be subscribed, and that a certain per cent. must be paid into the treasury before the corporation can do business as such. This amount varies in the different States. The purpose is to protect the innocent investor against organizations which are created for no legitimate business purpose.

Upon securing the charter from the State there are certain things which must be done before any business can be transacted. Up to this point all business transacted by the incorporators is done at their personal risk, as though they were members of a partnership. In order to shift this responsibility to the corporation, it is necessary to complete its organization. This is done by selling the required amount of cash stock, by the election of officers, and by the framing of a set of by-laws.

Due publicity must be given to all holders of stock of the time and place of meeting for the completion of the organization. Each stockholder is entitled to as many votes as he has shares of stock, and he may vote in person or by proxy. The organization is completed by the selection of a board of directors from among the stockholders. The number of directors is usually left to the incorporators, but frequently they are required to stipulate the number in their application for the charter. It is in the selection of the

board of directors that the business of the corporation is determined. The business ideas of the stockholders are reflected by the board.

After the selection of the board of directors the stockholders may frame the by-laws, fixing the powers and responsibilities of the officers of the corporation, or they may delegate this power to the board of directors, but the by-laws must not conflict with the existing laws. When these steps are taken, the active interest of the stockholders in the management for the time ceases. The board of directors take up the next step in the organization. They proceed to select a president, vice-president, secretary and treasurer, and such other officers as may be required by the articles of incorporation or by-laws, who are to be the responsible agents in the final organization and administration of the business. These officers are generally the heavy stockholders, and it is upon them that the responsibility rests for the final organization of the business, and in starting it as a going concern. In the meantime books have been opened showing a complete record of the different steps in the organization, and also a set of books for the record of stock, showing the amount of shares taken by each person, the amount paid in, and the transfers.

This completes the organization of the corporation as required by law. The corporation has now received the full sanction of Government,

and has become a juristic person, endowed with a continuous life until it is dissolved by due process of law. Before taking up the powers and activities of a corporation, we may indicate here the method of its dissolution. The law provides certain methods for closing up its business. This is done by presenting evidence of an adjustment of all of the obligations and the distribution of the corporate property upon the basis of the stock issued. After satisfactory evidence has been presented to the State authorities—or, in case of insolvency, to the court—the charter is surrendered, and the corporation goes out of existence. In the light of the law a corporation never dies except in case of the voluntary surrender of its charter, or through insolvency.

The powers exercised by a corporation are of two kinds: first, those which are expressly given by the charter; and, second, those which are implied from the nature of the business. It is empowered by the charter to purchase, hold, and convey such personal property and real estate as the business may require.

In order to complete the organization, the board of directors are empowered to appoint subordinate agents, fix their powers, and grant suitable compensation. The board may issue new stock from time to time, and enter into obligations and contracts which are essential to the transaction of the business. While it will be

observed that these expressed powers are exceedingly definite, at the same time much elasticity is permitted in carrying out the details of the business. The implied powers are usually restricted to those transactions which are necessary to the conduct of the business, and consequently differ with its character.

The classification of corporations is based upon the kind of powers which they are permitted to enjoy by the State. They are first divided into public and private. A public corporation is some division of the State endowed with limited powers in the administration of public affairs. A private corporation, on the other hand, is one organized for the conduct of private business ventures, and is given legal recognition in order to enforce full responsibility. Between these two classes are found a number of corporations which are generally termed quasi-public corporations. These are organized to conduct some business which is public in character, but carried on as a private undertaking. Examples of such corporations are water-works, street-railways, gas and electric-lighting companies. In many of the States private corporations are still further designated as domestic, foreign, and alien. A domestic corporation is now organized under the laws of the State where the business is conducted. A foreign corporation is one organized under the laws of another State, and an alien corporation

is one organized under the laws of a foreign Government.

A valuable feature of corporate activity, and one which throws considerable light upon its nature, is the kind of stock which it may issue. The object of issuing stock is obviously to acquire capital for carrying out the business policy. Connected with the sale of the stock arise many new and intricate problems. We have already noted that the investor acquires an interest in the business when he becomes a stockholder. The amount of stock which may be issued is left generally to the incorporators, although in some instances the statutes are specific. Obviously, the corporation ought not to issue stock beyond its ability to declare a reasonable dividend.

The capital stock is the sum fixed by the charter as the amount to be paid into the treasury by the stockholders for the conduct of the business and for the benefit of the creditors. This must be distinguished from the corporate property. The corporate property may increase or decrease with the conduct of the business, while the stock is fixed by law. All of the stock may not be sold by the corporation. The amount of capital stock issued may be only nominal; and, in fact, a large business may be carried on with only a very small capital stock. The persons who are to determine the policy of the business are those who hold the stock. No better illustration is found than the

recent reorganization of the Equitable Life Insurance Company. Here we find an enormous volume of business controlled by the holder of a very few hundred shares of stock. Other instances of a similar character might be cited. One case in particular has come to the notice of the writer, where a business of several million dollars a year is done upon a capital stock of $15,000. So that, in organizing a corporation, the amount of stock issued will depend, first, upon a desire to control the business policy, and, second, upon the amount of capital required to carry on the business. It is not infrequent that the capital stock is held by one or two individuals. In this case the corporate form of organization is chosen instead of a partnership in order to limit the risks and liabilities in the conduct of the business.

A subscriber for stock is a person who has agreed to take the stock of a corporation upon its original issue. A shareholder, on the other hand, is a stockholder, and is one who owns corporate stock. The stockholder has no legal right to the property of the corporation, except through dividend, or upon the dissolution of the corporation, or by an appropriate legal remedy for the protection of his rights. His rights to the property are finally determined by the stock he holds.

A share of stock gives its owner a right in the management, profits, and ultimate assets of the

corporation, and for this purpose is usually divided into various classes. The stock entitles the holder to a pro rata division of the profits and assets. Common stock ordinarily covers more than the material property. It represents often the intangible assets, such as trade-marks, patents, franchises, and other rights.

The preferred stock gives the owner a right to the dividends of the business out of the net profits in preference to other stockholders. Debentures represent usually the material properties, tangible assets, and working capital. This is one of the characteristic phases of modern corporate development. The holder has no voice in directing the business policy. The management rests with the common stock as a rule. The effect is to turn over the management of the corporate affairs to the common stock. The nucleus of the modern corporate capitalization is the intangible assets represented by the common stock. The preferred stock bears a stated rate of dividend, but is not collectable as a bond or a mortgage. It creates no obligation until the dividend is declared. The rights of the preferred stockholders depend upon the statute or contract providing for the issuance of the preferred stock. Generally speaking, in the absence of any controlling provision in the statute or contract, preferred stockholders stand upon substantially the same footing as the ordinary shareholders as far as their right to

participate in the control of the corporation is concerned.

Preferred stock gives the owner the right to participate in the general profits after the stipulated dividends are paid. Over-issued stock is that which is issued in excess of the full amount of capital stock authorized by the charter. Watered stock is that which is issued as fully paid up, when, in fact, the whole amount of par value has not been paid in. It purports to represent, but, in fact, does not, the money paid into the treasury. Watered stock is often issued to acquire a going capital without assessing the stockholder, but it may be issued, especially in the case of quasi-public corporations, for the purpose of distributing the funds among the original stockholders, and for the further purpose of keeping the annual dividends down to a point which will correspond with the current earnings of capital in other fields in order to avoid criticism. Obviously, the amount of watered stock will depend upon the present or prospective profits of the business.

In addition to the sale of stock, the corporation may increase its capital by issuing bonds. A mortgage given by a corporation is similar to that given by an individual. The usual form is a mortgage deed of trust, with a trust company as the trustee, to secure bonds issued by the corporation. In this case the trust company pro-

tects the interest of all the bondholders, collects the principal and interest as the bonds mature, paying the same to the bondholders, and, in case of default in payment, takes possession of the property and converts it into cash to pay off the bonds.

The stock of the corporation may be issued in several ways. The incorporators sell the stock until the amount necessary to complete the organization has been secured. After this preliminary sale the stock is often placed in the hands of underwriters, who sell it upon commission. The stock may be issued on the basis of a cash subscription. This is the simplest and safest method of disposal, and is the one usually employed. Stock may be issued, however, for property, labor, or some service performed in the way of construction work or legal services. These methods were subject to considerable controversy when first introduced, but are now accepted as a legitimate business practise.

Again, stock is issued in place of dividends, when those dividends are added to the permanent capital stock of the corporation. The method is employed when the capital stock of the company has not been fully issued, but cannot be employed to increase it beyond the limit fixed by the articles of incorporation. These are the usual methods employed by corporations for the disposal of their stock. The first and second are more gen-

erally employed, and especially the first. In certain kinds of enterprises often a considerable amount is disposed of for construction, engineering, and legal advice; still, the greater portion is issued upon a cash basis. A great many corporations do not place their stock upon the market. There are certain rules governing the admission of stock to the list which may be dealt in on the Stock Exchange, and the unwillingness of the directors to comply with these regulations excludes them from the Stock Exchange market, and forces them to private sales or to the curbstone market. The stock of a great majority of corporations is disposed of at private sale. One of the striking developments of corporations pertains to the method of capitalization. An analysis of the various ways of issuing stock and raising funds shows that the tendency is to separate the management from the ownership of the business. This deprives those who have furnished a considerable portion of the funds from any voice in the management of the enterprise. It takes the form of a trust in the hands of the owners of the common stock. This is particularly true of all forms of debenture.

This brief summary of one of the most interesting developments in law applicable to business will serve to bring before us the nature of a corporation, and to give some idea of its importance as a type of business organization. The

corporation was thus expanded to meet the requirements of a responsible organization as applied to business. But the more recent demands have brought about a further development of the corporate idea. As the partnership enables individual business men to unite, so the corporate idea enables further extension by uniting individual corporations under one central management. The corporation is the characteristic form of business organization, but it is not the only form.

It now remains for us to note the leading characteristics of this recent development in business. The growth of business has been characterized by consolidation and elaboration. We have found that the individual business man combines to form the partnership. The introduction of the corporation has permitted a still further development along this line. By combining a number of corporations within a given field of business, co-operation is secured. The most usual form which this assumes is the trust, known under various names. The purpose of this organization is to control prices, prevent competition, cheapen the cost of production, and, finally, to reduce the cost of administration.

The method of bringing this about is to unite the corporations of a given line of business through some agreement, written or verbal. The first important formal organization of this char-

acter was the Standard Oil Trust in 1882. With the success of this movement, there soon appeared the sugar, whiskey, cotton, oil, and starch trusts, and later other lines of business have been so organized, and the whole country has been gradually covered with a network of combinations.

The evolution of the trust organization has been a gradual one. It had its beginnings with friendly agreements affecting the mutual interests of the component corporations, such as the regulation of trade customs, listings, quotations, scale of prices, cost of advertising, and many other details. There was no change in the organization of the individual corporations under these agreements, but merely a friendly co-operation. Professional and business courtesies were developed into strong controlling factors. At times meetings were held between the representatives of the firms for the purpose of fixing prices, and of organizing common distributing agencies. A good illustration is the agreement entered into by railroads for the purpose of fixing passenger and freight rates.

The next step was to organize more formally for the control of the quantity and price of the output. These agreements were usually put into writing. This is a method frequently employed by wholesalers in fixing prices to retailers. Penalties are instituted and premiums offered for the preservation of these contracts. Such institu-

tions as the American Tobacco Company and Whiskey Trust have extensively employed these methods. We now pass to a still more formal understanding, which preserves the individual corporations, but at the same time creates a common machinery to carry out more effectively the policy of the combination. This is done by creating a trust company to hold the stock, or a majority of it, for which trust certificates are issued. The original stock of the corporation is often secured by a trust mortgage to the extent of the valuation of the factories, which is issued to each corporation entering the larger organization. At times the trust certificates are issued for the corporation without any mortgage. In each instance the principle is the same, and the method employed will depend upon the degree of confidence reposed in the trustee.

We now pass to the permanent consolidation whereby the individual corporations lose their identity and become a part of the larger organization. This is brought about by leasing, renting, or buying the property of the smaller corporations, so that the consolidation is completed either by lease or by ownership. Sometimes the component corporations are managed independently, and at other times are controlled strongly by a central administration.

The organization of the trust is brought about by drawing a trust deed or articles of agreement

under which a charter is usually taken out, followed by a detailed valuation of the property of the several companies as a basis for the distribution of the trust certificates. A president and board of directors are elected and a staff of officers provided, after which the capacity of the various plants is carefully ascertained and a policy of production and selling agreed upon. Some factories are selected to run at full capacity, while others run at partial capacity, and some are even closed. For instance, the Whiskey Trust closed sixty-eight out of eighty factories.

On account of the strong sentiment against these organizations another step has been more recently developed to bring the allied interests under one control. This is accomplished by transforming the trust into a corporation. The trusteeship is converted into a corporation by converting the trust certificates into stock. The trustees then become directors of the new corporation, and little or no change occurs in the organization of the business as a whole.

As a result of this evolution we have the following organization of large combinations. At the head of the organization are the president, board of directors, and staff of officers, as required by law. The board of directors is divided usually into two departments—one concerned with the financial affairs, and the other with the technical and administrative side of the business.

These are further subdivided into committees on sales, purchase, technical supervision, advertising, selling, etc.

The relationship which each individual company bears to the larger organization will depend upon the conditions of the agreement. In some instances each corporation is permitted a large degree of independence in matters of a local character, while the larger organization takes up the administration of those matters of a general character. Very frequently the central administration buys the material, fixes the selling price, and apportions the larger orders among the firms. Each component corporation is permitted to take small orders directly, and to decide upon some of the details of management. They keep in constant daily communication with the central office through regular reports. We find in practise varying degrees of centralization, and no fixed rules can be prescribed.

It will thus be seen that there has been gradually evolved a type of organization which has taken the simple corporation as a basis, beginning first with loose and often verbal friendly agreements, and gradually passing into more formal and compact organizations. We find that in some instances the component organizations are independent going concerns, while in the other instances the consolidation has gone on to the extent of destroying their administrative identity,

and has transferred the supervision and control to one central organization. The purpose of these organizations is essentially the same in all instances. They have united their capital and business ability for the purpose of regulating production and distribution.

The form of organization is probably a secondary consideration as measured by the results obtained. The organization has been evolved to meet the requirements imposed by legislation. The primary purpose has been the control of production and distribution, regulation of prices, and other features of competition, and to secure administrative economy. It is true that administrative expenses have been materially reduced, and in many other ways the efficiency of the trust is shown. It has advanced at present to the stage of a large federated corporation, tending more and more to destroy the identity of the component parts.

It is impossible at this stage of the evolution to determine the ultimate value of the trust as a type of organization. It has changed its form to meet public criticism and hostile legislation without a change in its real intent and purpose. From the point of view of business organization the efficiency of this more comprehensive type is not always easily ascertained. There is undoubtedly a demand for large business organizations. It is also obvious that in many instances these

large business units cannot be successfully split up into smaller ones, if the best results are to be obtained. From the point of view of business it is equally apparent that the organization should be utilized as freely as is consistent with justice in trade. Our industrial life seems to move irresistibly toward consolidation, and it is natural that the corporate idea should be used to bring this about.

A careful distinction should be made between those business consolidations based upon complete ownership of property and those based upon a union of management. A consolidation which grows out of the purchase of different properties overcomes at least the legal objections, but when it takes the form of a consolidation of management, the legislature and courts have interposed. Various attempts have been made to bring about a union of interests by establishing a central organization, or selling agency. From the point of view of each individual business there is no doubt about the efficiency of this plan. It may not, however, be legal or good public policy.

It is an important fact that the corporation is the most highly perfected mode of organization recognized by the law and approved by business practise. It is essentially a modern creation. It has solved the problem of business risks and liabilities, and permits an elastic administration of business affairs.

By way of conclusion, we may briefly summarize the advantages of a corporation in business as compared with the non-corporate organizations. The corporation makes possible an unlimited number of stockholders, combined with the limited authority of the directors. We have seen that the partnerships are usually unlimited, because each partner may do a great many things for which all of the other members are severally liable. Not so with the corporation. Those persons who are authorized to incur debts and make contracts are known to all stockholders and to the public by virtue of the law. The directors are the persons liable, in case they attempt to transact any business not fully granted or implied in the articles of incorporation or the by-laws. But, unless they act outside their powers, their acts do not bind any one except the artificial legal person created—the corporation. Where "good will" is large and expansive, corporate organization is most useful. It permits the increase and decrease of capital commensurate with an expanding or decreasing business.

The corporation makes possible a union of capital without a union of service on the part of the stockholders. It permits the investment of funds from many sources for conducting business upon a larger scale than is possible to the individual investor. It permits one to invest in many enterprises and yet take no part of the

management of the business and incur no liability for its debts. The stockholder acquires the right to determine who shall manage the business, but when this function is performed, his personal attention to the details of business ceases, unless he becomes an officer of the corporation. A capitalist may have his money invested in a hundred enterprises, and he may give no attention to the details of management. The corporate type thus permits the stockholders to turn over the organization and the administration of the business to the directors who are elected for that purpose. This is a most important and vital feature of the corporation as a type of business organization. The corporation has better facilities for securing capital, since it may issue stock, sell bonds, and borrow money upon its earnings and upon its property.

The corporation is a continuous organization. It never dies except by failure or dissolution. In the case of a partnership, the retirement of a partner, or the admission of a new one, usually involves the reorganization of the business. But not so with the corporation. Stock may be bought and sold and changed upon the transfer-books of the corporation without any change in the organization, or the business policy. This change of interest, through the sale and purchase of stock, is one of the most important features of the corporation from the point of view of the

management of the business. It permits that continuity so necessary to successful results. No abrupt and hazardous changes of policy need take place, unless some individual acquires a controlling interest in the stock, and then such changes cannot take place until new directors are selected, or by the consent of the old ones. It is a most valuable feature of the corporation that a stockholder can retire without disturbing the business, and that this can be done without the consent of other stockholders, unless especially prohibited.

The title of the property is in the corporation, and is not affected by the death of any holder of stock or by the sale of stock. No individual stockholder has a right to the property except on the basis of the stock which he holds. In like manner, the debts of the corporation do not follow the stockholders, unless they have failed to pay for their stock, in which case they may be liable for the unpaid balance, or unless some special liability has been created by statute as in the case of banks. But ordinarily the debts of the corporation do not affect anything but the corporate property, or the earnings of a corporation as a going concern. The affairs of the corporation may be taken over by a receiver, and the property disposed of for the benefit of the creditors, or the business may be conducted for the purpose of securing the funds necessary to satisfy their demands. It is at this point that

the difference between the partnership and the corporation is most apparent.

It thus appears that the advantages of the corporation over a partnership or the individual business man, as a form of organization, are very marked. Where the partnership has been found clumsy and dangerous in large business enterprises, the corporation, with all of its elastic features, has been found fully capable of meeting the demands placed upon it. And while the corporate laws are in some respects lax and insufficient, particularly relating to the sale of stock to ignorant and innocent purchasers and to the control of watered stock, yet the fact remains that the corporation is the most advanced type of business organization and administration universally recognized to-day by the law and by business practise.

PART II

PRINCIPLES OF ORGANIZATION

A.—ORGANIZATION OF EXTRACTIVE INDUSTRIES

IV

BUSINESS ASPECTS OF FARMING

We shall begin our account of the organization of business with a brief discussion of farming. From the point of view of organization farming is simple, but on the other hand, farm management presents many exceedingly complex problems. No other line of business affects so large a proportion of our population, or represents so large a cash value in output. In the United States in 1900 there were 5,739,657 farms, representing an enormous investment. The number of farms shows that in this field the small business units prevail. Although the management of crops and stock have received some attention, little has been written concerning the commercial side of farming. It is the purpose of this discussion to point out those elements entering into farming as a business distinguished from the cultivation of the soil.

In the popular sense a farm means a tract of land devoted to cultivation. This is also the legal conception. The idea of cultivation is inseparably connected with the conception of a

farm in law and in practise. In its broad sense the business of farming has two distinct phases—the production of crops, and their marketing. This latter phase is capable of indefinite expansion, and may take the farmer into the local market, or even to the primary market. The farmer is forced by reason of his situation to add to the business of cultivation that of marketing. He must in most instances be interested at least in its initial stages.

We aim to confine our discussion to farming proper—that is, the organization of agricultural production. There are a number of elementary, but far-reaching considerations involved in this phase of farming. We shall employ the term farming according to the American usage, which refers to the actual cultivation and management of a piece of land. One of the first business propositions coming before the farmer is to determine the size of the farm that will be most profitable for his kind of farming. In the early stages of agriculture in the United States it was customary to farm on an extensive scale. Land was cheap, and it was more profitable to plant a large acreage of new soils than to attempt to maintain and improve each piece of land through intensive cultivation. In some sections peculiar labor and crop conditions developed land-holding and cultivation on a large scale. In fact, where the one-crop system prevailed, the large farm

was the rule. Under these conditions the farmer considered the size of the farm more important than the quality of the soil, or the manner of cultivation.

Certain forces have, however, been at work to break up these large holdings into smaller farms. The pressure of population in the Middle West, along with the growing appreciation of closer cultivation, and the loss of capital and slave labor in the South, have tended to reduce the acreage of the farms. In general, the methods of mixed and intensive cultivation have made the smaller farm more profitable. More recently greater attention has been given to the selection of soils for special lines of farming, and a larger interest in scientific cultivation has followed. In short, wherever intensive cultivation is carried on, the tendency has been to divide the large holdings into smaller farms.

Farming of necessity is a small business. Farming on a large scale is the exception. Each unit of management represents a small capitalization. The organization cannot be made complex and extensive by uniting hundreds of men and large capital under one management, as in the case of the factory. Efficiency of management is impaired with the increase of the size of the farm, because close personal supervision, so necessary where larger bodies of men are employed, is lost. The plantation and ranch sys-

tems are attempts to apply the factory organization to farming in a limited way.

In selecting a farm, nearness to the market and fertility of soil are controlling considerations. A truck farm should be nearer the market than a live-stock farm. Mistakes are frequent in the selection of equipment and stock. These should be made with reference to productivity of the land. Time may be saved and the quality of the output of the farm improved and made more profitable. Too little attention has been given to labor efficiency, both as to quantity and quality; but, as farming becomes more advanced, the latter becomes more important.

The character of the farm organization will be determined to a considerable extent by the size of the farm, as well as the particular kind of farming which is carried on. In determining the minimum size of the farm, the family is usually taken as a basis. From this point of view the minimum farm will be one which will support a family, and can be cultivated by it without additional labor. The thought is that no piece of land can be considered as a unit of organization and management unless it yields a sufficient return to support at least one family. From this point, however, the size of the farm may be considerably expanded as a unit of organization. For instance, instead of the proprietor devoting his time to the labor of cultivation, he may con-

fine his activities alone to the management and employ others to do the work of cultivation.

Under proper management this plan will enable a considerable acreage to be cultivated under one organization, but obviously there is a limit to the size of the farm from the point of view of profitable management alone. Possibly the best method of determining the profitable size of the farm is to inquire statistically into the farms of the present day, assuming that the present average size is the result largely of profitable returns upon the investment. It must be assumed that the size will be determined by financial results under a definite system of management. Other causes may be at work, such as speculation in land, which is associated with the development of a new country, but in the end the standard of efficient management must prevail. The size of the farm must, then, be measured by the profits accruing from it, just as the size of the factory will be determined by the volume of its business. The statistics cited are often based upon holdings, whereas the proper distinction should be the unit management, for often large holdings are in groups of single farms, and are so managed. But it is impossible to state exactly the size of a farm which may prove profitable under one management.

From 1850 to 1900 the average size of farms in the United States decreased. In 1900 the

average acreage per farm for the United States was 186.6, while the average improved acreage was 72.3. In the West the farms are larger than in the eastern and southern sections, due to peculiar climatic and economic conditions. A number of factors determine the size of a farm as a profitable business venture. Among these are climate, whether intensive or extensive cultivation is followed, the kind of crops, labor, equipment, and talent for management. It goes back finally to the organization and managing ability of the farmer. It is determined by his power to combine these various elements of soil, equipment, and labor into an effective organization. Profitable holdings for speculative purposes may operate to keep up a large acreage for a time, but there comes a period when this must be divided into farms for actual cultivation.

The profitable size of the farm will depend to a great extent upon the efficiency of the farmer or the manager. It is obvious that a farmer with the proper conception of farming as a business will handle the same acreage with better results than one who does not properly appreciate this side of farming. In the management of crops and in their marketing the business efficiency of the farmer is marked. This affects the size of the farm as a basis of profit. This efficiency may take the form of intensive farming, or production, and in that case it will tend to decrease the

acreage. It may also take the form of the efficient handling of the commercial side of the farm. In this case it will tend to increase the size of the farm.

Again, the size of the farm will depend upon the kind of farming to which it is devoted. For instance, stock-raising requires a larger acreage than tobacco-growing. In other words, the maximum efficiency is reached on a smaller acreage in growing tobacco or cotton than in stock-raising, or in cereal farming. This is due to the more intensive methods which may be employed in the former cases. A larger expenditure of labor per acre is required, and the yield is correspondingly greater in cash value per acre. In order to determine whether a system of intensive or extensive farming is employed, some unit of measurement is necessary. It is generally determined by the amount of labor, capital, and management that are devoted to a given acre. Where these are small, the farming is extensive. It is obvious that no hard and fast rule can be laid down in deciding which of the two systems is in use.

From the point of view of organization the systems of farming may be divided into two classes: direct management, and tenancy. Direct farm management is carried on by the proprietor or a manager. In most instances the manager is the owner. This system is applicable to small

as well as to large farming, and has the advantage of uniting the interest of ownership with that of management, and the profits of both fall to the same individual. The proprietor may even perform the labor, or he may have a sufficient acreage to enable him to devote his entire time to management. Of the total number of farms of the United States 63.7 per cent. are managed wholly or in part by the owners, while the system of tenancy is represented by 35.3 per cent. This shows a slight increase in the latter system since 1880. Only one per cent. of the farms are directed by salaried managers.

In former years, in the West and the South, we find extensive holdings cultivated under the system of direct management, and even to-day we find in these sections the same system under a modified form. It does not always follow that the owner undertakes directly the work of management, but he is often represented in this capacity by a manager. Under this system the manager is paid a salary, and stands in the same relationship to the owner of the farm that a manager of a factory stands to the director of the factory. A central office is usually established for the purchase of supplies, the sale of the products of the farm, and the supervision of its operation. Where the farm is of sufficient size the general manager has under him superintendents who direct the work of groups of laborers,

or who manage certain parts of the farm. This system was especially in vogue in the cotton and tobacco belts of the South during the days of slavery, and is still found there in a modified form. The same system prevails on the large wheat and cattle ranches of the West. Here we find a degree of specialization in the organization of the labor force akin to the system so elaborately carried out in factories and commercial enterprises. Naturally, the principle of the division of labor cannot be so successfully applied to the farm as in the case of other business organizations where the work is uninterrupted by the seasons of the year. This system of direct management is especially adapted to the one-crop system of farming, for the reason that the farm operations are constantly repeated, and the working force becomes familiar with their duties.

The second system of farm management is the renting or leasing system. It assumes usually two forms—the cash, and the cropping system. In either case the identity of ownership and management is lost, although it may be safeguarded in a measure by the provisions of the contract. This method of farm organization is dangerous, and likely to become ruinous for the reason that it too often disregards the most essential feature of successful farming, which is the maintenance of the productivity of the soil. For even the owner is led to disregard his own interests in the

long run by exacting such high rents that the renter is compelled to take everything possible from the soil, even to the point of exhaustion. For many reasons the tenant system is constantly fluctuating. This is due to the fact that prosperous farmers frequently retire, and hold their farms as investments, and also because some investors look favorably upon farm lands as a form of profitable investment for normal returns upon capital. Out of the total number of farms in the United States 35.3 per cent. are cultivated by tenants. This per centage has increased during the last few years. Out of a total number of rented farms in the United States, about one-third are rented on a cash basis, and the remainder on the cropping basis. It seems that the predominant system of renting is by shares, except in New England. In the West the cash system is growing. In the South the cropping system is the usual mode, especially in the cotton belt.

Unless the system of renting can be combined with the system of supervision by the owner of the farm, or by offering inducements to renters to maintain its general productivity, it will in the end prove disastrous. An instance of combining supervision by the owner with that of the renting system is found in the management of a tract of 35,000 acres in northern Indiana. This large holding is divided into about 200 separate farms,

each with a full quota of buildings. These farms are then grouped into districts over which is placed a superintendent, who is directed from a central office. Each farm is then rented on a cash or crop basis, generally the latter. The contracts with the renters often stipulate the kinds of crops to be planted and the method of marketing. Provision is made by the owner for the transportation of the output of the farms to the Chicago markets. Each superintendent of a given district makes the rounds of his farms, to watch over their cultivation, and to see that the contracts are faithfully fulfilled. This instance is exceptional, but shows the possibility of combining a system of supervision with that of renting. By reason of the hard and fast contracts the individual renter is little more than a hired laborer, although his returns are determined by his own exertions.

Where the crop system is used, various methods are employed to fix the rents. A common method is to take a share of the crop, usually one-third or one-half, to be delivered in the bins upon the farm or at the nearest local market. Various methods are devised to determine the share going to the renter and to the owner of the farm. Where the cash rent is employed, one of two plans is usually followed. The amount of the rent is either fixed at a lump sum for a year or a series of years, or the farm is gone over, and the

rent of each lot is determined upon the basis of acreage and productivity. The cropping system is probably fairer to the renter, and gives the landlord a firmer control over the management of his farm. As a means of fixing exactly the shares of the renter and the owner, this method has obvious objections. However strongly it may appeal in theory, it is difficult to work out in detail. Most generally the produce is divided upon a market basis. But formerly it was customary to make the division before the crop was harvested. For instance, corn was divided by rows. In the case of small grain the division was generally made as it came from the thresher. Because of these crude methods, with their involved details, the more recent practise is to use the cash system.

But the cash system of renting does not appeal to the landlord because it threatens the productivity of his land. For this reason the more progressive landlords place their farms in charge of tenants, who are also nominal managers. They are required to put some capital into stock and equipment. In this way they are more than tenants. They become partners, and profits and losses are distributed on this basis. This system has much to commend it from the viewpoint of both interests. It is, in fact, the principle of the partnership applied to farming, for it is the combination of the systems of management through

a salaried superintendent and the renting in its pure form.

The greatest danger of tenant-farming is its tendency to become a system of soil robbery. It is exceedingly difficult to safeguard the farm against the ravages of the tenant system. Tenants too often are not successful farmers, or else they would own their farms. The tenant system has been aptly characterized as "mine-farming," for the reason that it takes the elements from the farm, and carts them to the market without returning anything to sustain the fertility of the soil. This is particularly the case of the one-crop system which prevails so generally in the cotton and wheat belts. A capitalist who loans his money can secure the return of his loan unimpaired, but the owner of a farm who rents it cannot consider himself so fortunate. He gets his acreage back, but too often minus the fertility. Consequently too great care cannot be exercised in stipulating the character of cultivation, the rotation of crops, and the maintenance of soil fertility. For the reason that the share system enables the owner to protect his land against mismanagement, it is generally preferred to the cash system. It comes nearer uniting the management with that of ownership. When these considerations are not present, the cash system is preferred in order to secure the fixed returns. From a business point of view it is a wholesome

thing to find that direct management and the share system largely predominate.

The successful cultivation of the crops does not alone constitute good farming from a business point of view. Too little attention is given by the farmer to the commercial aspects of the business. Very few farmers keep close watch over the financial side of their business, and pay too little attention to the cost of producing their crops, or to the study of the markets for the purpose of determining the kind of crops to be cultivated, and also the best markets and the time or seasons of their marketing. It has been shown that the one-crop system leads to an early sale of the crop in order to realize cash and to avoid the risks of storage. The crop is too often put upon the market when the prices are low. On the other hand, mixed farming has many advantages from the point of view of prices, sales, and the preservation of soil fertility.

Ultimately the farmer must receive cash for his crops in some form. With the one-crop system it must come from the sale of a single crop, while in mixed farming, it may come from several sources. Surplus-crop farming is likely to prove disastrous, while farming for supplies is not so hazardous. Surplus-crop farming is hazardous in that it leads to soil exhaustion, and often to low prices. The Illinois Department of Agriculture estimated that the corn crop of 1896

lost the producers of that State $20,000,000, and in 1887 $17,000,000. The prevailing prices were below the cost of production, and, furthermore, because the crop was marketed as a surplus crop rather than as a supply crop. This is precisely the position of the cotton-grower of the South, and the all-wheat farms of the West. Surplus farming has proven disastrous in the cotton and tobacco belts of the South.

The farmer may employ competing crops, or one crop by the field system. Where the latter is employed, its extent will depend upon the number of crops used in the rotation. In most instances three crops are employed. The old practise of allowing a field to lie fallow has largely ceased. In its place have been introduced fallow crops and stock-raising. Special farming does not mean the growing of one crop only. It does not exclude rotation, but refers rather to the selection of those crops best adapted to particular soils and markets. It is expert farming. A dairy farm may employ rotation to improve the fertility of the soil. Special farming is obviously subject to more dangers than mixed farming, which is the raising of a little of everything, without emphasis upon any one crop.

In selecting and cultivating a farm, the maximum return is sought over a series of years. Like other business activities, the farm products are converted into cash; but values may be added

in other ways. Selling crops are not always in the end the most profitable. Commercial farming must be carried on with reference to the market and continued fertility of the land. Naturally, the goal of successful farming is found in the selection of the best soil, live stock, equipment, labor—all operated under skillful management.

The lack of capital for farming operations, combined with the practise of renting the land on a cash basis, has tended materially to impoverish the soil. In most farming sections the farmer conducts his business with his own capital or upon credit. In case he borrows money for the stocking of his farm, or for current expenses, it in no manner affects his freedom in marketing his crops. This condition prevails especially in the prosperous farming communities, where the mixed system of farming prevails; but where specialized farming is the rule, and particularly the one-crop system, such as wheat, cotton, and the grazing-farms of the extreme West, we find that it is often customary to advance money upon the output of the farm as a security. It is customary for live-stock merchants and commission men to advance money upon live stock before it reaches the market. This "cattle paper" is considered good security, and is negotiable at the money markets. In wheat and cotton-farming this practise also prevails, but it is especially in

the South that this system has worked disaster to the farming communities.

The devastations of the Civil War swept away the surplus money of the planters, and compelled them to rent their lands to shiftless tenants upon a share basis. The planters had no money, and were compelled to cultivate their lands upon credit. This capital was secured in two ways—by cash advanced by the cotton and tobacco merchants and dealers, or by extension of credit to the farmer at the country store, guaranteed by the owner of the land. In either case the person who provided the cash or credit for provisions exacted a contract, which was often more than a security for payment of the debt. This contract usually goes so far as to specify what the planter shall grow, and the amount of acreage which he shall cultivate. In addition to this, it calls for a delivery of a certain share of the crop to the person who advances the credit, or to others designated by him. Thus it will be seen that the crop mortgage, as practised especially in the cotton belt of the South, furnishes a basis for the control of the operations of the planter, and also, in addition, the sale of a specified percentage of his cotton.

This practise does not generally prevail in the north-central farming communities of the United States, on account of the surplus capital which the farmer has accumulated, or his ability to

borrow cash upon security without regard to the manner in which he shall market his products. The system in the South has made the planters largely dependent upon the country merchant and money loaners. In a great many cases the renter has little left after the planter has taken his share and the merchants have received their quota for provisions. There are, however, two influences which have tended to overthrow this method of renting. One is the growing surplus capital of the renter, and the second is the loss that country merchants and money-loaners have sustained by the failure of crops.

The farm organization of the cotton and tobacco belts is so peculiar that it requires a more specific treatment. In more recent days the farming in the South has become more diversified. In order to appreciate the present situation in the South, it will be necessary to revert briefly to the conditions prevailing before the Civil War. The presence of slave labor and the development of a land-holding class gave to Southern agriculture a unique form of organization. The plantation became the ruling form of agricultural organization. This was especially true of tobacco, cotton, sugar and rice-growing. While they differ somewhat in detail, yet in general these plantations were organized on similar lines.

The plantation system of that time employed a considerable acreage of land under one manage-

ment, and was to a great extent a self-sustaining organization. Not only were these products of the land marketed, but many of the things needed were manufactured upon the plantation. Before the War the average size of a plantation was about 400 acres. The Southern planter was in a sense a captain of industry; he was the owner and manager of a large business, with all of its numerous details, and large rewards came to those who possessed the skill to organize and manage these estates. Slavery tended to widen the area of the plantation. The large plantation was considered the safest and most productive form of investment. Added to this the growing number of slaves to be employed, the necessity of replenishing exhausted soils, increasing needs for pasture, and we have the primary economic causes which tended to enlarge the plantation.

The owner usually hired a manager and superintendent, who directed the operations of the plantation. He also had charge of buying supplies and marketing the crops. He determined the crops to be grown, and directed and supervised the cultivation, planting, etc. The labor force was grouped into gangs and placed in charge of a leader or superintendent. By this method an organization of considerable importance was developed. It involved in a limited form the division of labor as worked out in the

factory system. This system of organization was well adapted to the conditions of agriculture in the South during the slave days. It was unquestionably more effective than any system of renting to small farmers, which prevailed in some instances. The system of direct management, through a general manager and superintendent, retained the identity of ownership and management. The plantation system must thus be considered as eminently adapted to the labor conditions, as well as the form of land tenure, which prevailed in the South at that time.

The Civil War brought about two conditions which have affected in a far-reaching way the agricultural organization of the South. In the first place, it swept away the surplus capital of the planters, and, in the second place, it converted the slave into a free and independent laborer. This latter was probably more far-reaching in its influence upon the plantation system than that of lost capital. The capital could gradually have been replaced, but the character of the plantation system was virtually transformed with the loss of the discipline, which was secured through the institution of slavery. The abolition of slavery, then, not only destroyed an economic institution of great importance to the South, but it also put an end to an agricultural organization of considerable age.

The planter of to-day is compelled to depend

upon the labor of the negro, or to rent his farms out in parcels to descendants of his former slaves. These two considerations, together with the fact that the soil has become impoverished through the one-crop system, confront the farmers of the South with an uninviting situation. A permanent and fairly efficient labor organization was destroyed, and in its place was put a shiftless and unstable laborer, The free labor and loss of capital have destroyed the plantation system of the ante-bellum days. In some of the Southern States the number of farms has quadrupled. In Texas the number has increased one hundred per cent., while in Georgia, Alabama and Mississippi the increase has been as high as two hundred per cent.

These conditions have brought about radical changes in the methods of agricultural organization. As a result, the farms have decreased in size, and are rented largely to negro tenants, especially in the cotton belt. It was for these reasons that the plantation system collapsed after the Civil War. The downfall of slavery compelled a readjustment of all industry where labor was needed. It would be difficult to find in any agricultural community so wasteful a system of farm organization and management. The owner of the soil now seeks to procure as large a return as possible from his impoverished lands, and the merchant, on the other hand, seeks the

largest return possible for his provisions; and all must be met by a share of the tenant's crops. This fostered the cropping system in the extreme. There is no doubt of its bad results upon soil and tenant in the cotton and tobacco belts. It becomes here often a partnership in which labor is given without hire, and capital is advanced without credit, for the reason that crop failures result in complete losses to all concerned. On account of the scarcity of capital for farm operations, it was necessary to make the crop the basis of credit. In order to make this secure, the Southern States generally passed stringent lien laws to enable the tenant and landlord to secure advances of money and credit. All forms of farm property are subject to these laws, but the crop lien is especially important. This strengthens the control of the merchant and money-loaner over the planting of the crop, and vitally affects its marketing. This is especially true of the cotton belt. It is estimated that fully nine-tenths of the cotton crop is sold subject to supply liens.

Cotton and tobacco are to-day the most important crops of the South. The demand for a surplus capital has compelled the planting of these crops from year to year without regard to rotation. Provisions must be bought from the country store, which has tended all the time to drain off the surplus farm earnings of the South to those sections which produce the provisions,

and equipment for the operation of the farm. The tobacco planters are to-day more independent of the system of crop liens than the cotton planters. They are gradually building up a working capital which gives them relief.

To-day the following methods of agriculture organizations prevail in the South. We have, first, the cultivation of the land by small farmers; second, the lease of larger holdings to small tenants, with the exclusive management by the owner, or by the use of the crop system; third, the larger estates still operated under a system somewhat similar to the plantation of the slave days. The second method seems to be the prevailing one for the reasons previously noted. The farm contracts which are employed generally in the South contain the following provisions. The landlord may furnish the land and mules and receive one-third of the crop. In this case he advances the supplies, and arranges the credit for provisions with the merchants; he may furnish the land and mules, and stipulate the quantity of supplies, and divide the crop; he may contract for labor by the year, and furnish the supplies; or, finally, he may rent the land for a fixed quantity of cotton, for which he usually receives about three bales per thirty acres. Under these conditions the tenant is between two iron-clad contracts—the one given to the owner of the farm, and the other to the local merchant who supplies

him with provisions. It will thus be observed that two influences have brought about the tenant system in the South. The one is the subdivision of land, and the other is the free negro, to whom the estates have been parceled out for cultivation. The owners of the large estates could not cultivate or sell them, and were consequently compelled to divide and rent them. Gradually the farmers are acquiring a surplus capital, which will doubtless gradually free them from the ruinous system of agricultural organization which has prevailed since the Civil War. There are some of the indications that the plantation system will grow in favor as that system of farm organization best suited to the conditions of the South.

The labor problem upon the farm is often difficult to solve, especially during the harvest seasons. The difficulties are particularly great in the cereal and cotton belts. The farmer is not in a position to employ sufficient force the year round to enable him to harvest successfully these crops, and so it often happens that in the cereal belts it becomes very difficult to secure a sufficient labor force to harvest the crop successfully. The methods of compensation of labor upon the farm are usually by the day, or the month. The steady laborer is obviously hired by the month, while the temporary laborer is employed by the day.

Another problem of considerable difficulty which confronts the farmer is that of equipment. In most lines of business the same equipment is employed throughout the year, but the farmer is compelled to invest his capital in expensive equipment which is used only for a short period. For instance, he invests in an expensive reaper, which is probably used for a period of two weeks, and in mixed farming more frequently for less time. Throughout the other periods of the year this machine is idle, and is subject to the rapid depreciation incident to unused machinery. The rule is that the machinery lies idle the greater portion of the time. Upon this idle capital, which is equal to about fifty per cent. of the value of his land, the farmer must make his profits. The same is likewise true of a large portion of the farm itself, especially where the one-crop system prevails.

These conditions render the commercial aspects of farming peculiarly difficult. The farmer is compelled to make individual operations profitable in order to carry over the year a considerable investment which is tied up in idle machinery and land. These things are not usually considered in their proper light by the farmer, and for this reason farming becomes often a losing business. But too often the farmer is unaware of this situation, because of his negligence in keeping proper financial accounts and records

of his business transactions. In fact, there is scarcely a class of business men so negligent in this respect. Cost-keeping and accounting are almost unknown among farmers. However, this situation is improving since farmers are coming to realize more and more the value of a complete record of their business transactions.

This review of the most important features of farm organization suggests some of the difficulties which confront those engaged in this line of business. While farm organization is simple in itself, the peculiar influences which surround it renders it one of the most difficult and hazardous of all business ventures. This is not only due to hazards which are associated with cultivation, but also to the character of the investment, and the variety of operations which each farmer is compelled to carry on in most instances. In recent years, however, great improvement has been made in farm organization and management.

B.—ORGANIZATION OF MANUACTURING

V

FACTORY ORGANIZATION

In the foregoing chapter we have described the organization of general farming. We now pass to the organization of the manufacturing business. Manufacturing is the transformation of a given product into new commodities. It usually refers to the changing of raw materials into finished products, but it may also mean the conversion of partially finished products. New values are added to the commodity mainly through additions of capital and labor. Accurately speaking, the function of the manufacturer ends with the completion of a commodity; he may, however, engage in the additional work of selling the output. Properly considered, this latter belongs to distribution, or the commercial phase of manufacturing. In our treatment of manufacturing we shall confine attention first to the organization of the factory, and then to the commercial aspects of the business, for the reason that the factory itself is the primary consideration before us. The commercial side of the business may have an elaborate or nominal organization, depending upon the extent to which

the management engages in the distribution of its output.

It is generally conceded by economists that the factory system is one of the most important institutions of our modern industrial life; its development has brought far-reaching changes in our industrial system as a whole. Not only has it made possible the production of varied commodities, but it has also introduced a type of business organization capable of great specialization. With its development have followed many changes in the larger field of business organization. The factory system is the application of mechanical devices, assisted by labor and supervision, to the manufacture of commodities. This means the grouping of labor and machinery into divisions for the carrying forward of definite kinds of work. It is this division into departments which gives the factory its peculiar position in business organization.

The factory system had its origin about the beginning of the eighteenth century; previously manufacturing was carried on through simpler methods. Historically, three systems have been employed, and these have struggled, so to speak, for survival and supremacy. The first and simplest form is the handicraft system. This is based upon individual effort, and implies the use of little or no machinery. It fails to expand into any

well-organized unit, and is found where manufacturing is in its initial stages.

The second is the household system of manufacturing. Here the family is the unit of organization. Under this system the family devotes certain seasons of the year and times of the day to the manufacture of some product in connection with the occupation of the farm or shop. These operations might continue through the year, but were generally associated with some other business of primary interest. A more elaborate machinery was employed, such as the hand-loom and other similar inventions.

Finally, the third system is the factory organization. It ushered in the so-called industrial revolution, and was closely identified with certain inventions in the manufacture of cotton and woolen goods. A great impetus was given to manufacturing by the invention of the steam engine or other forms of power, which made possible the location of factories at a distance from water-power.

The first two methods of organization are simple and wholly inadequate to the needs of our modern industrial life. The factory system makes possible the manufacture of commodities in larger quantities and on a more varied and economical scale. The dominant feature of the first two systems is the individual hand work with simple machinery, while the dominant feature of the

factory system is the large use of machinery and power, combined with the specialization of the labor and administrative forces. It made possible an intensive organization, and brought the individual and isolated workman of the household and handicraft systems into great organizations, dominated by one ruling spirit, and subordinated in all activities to one management. By any unit of measurement the maximum production of the factory system far exceeds that of the other two methods of manufacture. Everywhere the old trades and gilds were broken up, and gave way to the great factories of our present day. No longer the individual laborer was working essentially for himself, for he now becomes a manager, foreman, or laborer, and enters an organization which submerges his individuality.

The purpose of the factory is to divide and combine the labor and administrative forces and machinery into definite units of organization. The individual thus has no control over himself except that he, of course, retains his right to withdraw from the organization. He must be present at a certain time, stop work at a given time, and modify his individual inclinations so that they will in no manner impair the efficiency of the organization.

On the other hand, he is relieved of certain responsibilities incident to the business. He has no risks of investment and assumes no responsi-

bilities in the management of the plant, except in so far as he may be entrusted with work as an employee. He becomes a specialist. His responsibility is narrowed and intensified. In other words, the factory is the expression of the individual workman only in so far as he contributes to its efficiency, and the combined effort of the labor and administrative forces is expressed in the quality of the factory output.

With the rise of the factory system a clear and definite distinction between managing ability and labor was gradually introduced. The factory organization created a demand for large units of capital. The capitalist class brought into the field an entirely new group of workers who were to assume the responsibilities of organization and management. But, still further, the factory called for a large body of laborers, who were to assume none of these responsibilities.

The factory system is a universal mode of production; it is used in all kinds of manufacturing. It cannot be considered as an ultimate type of organization, but to-day at least it is dominant. The form of organization which may take its place is, of course, a matter of conjecture. New relationships between labor and capital are constantly suggested and advocated.

We can now turn to a discussion of the more important problems connected with the organization of the manufacturing business. One of the

most important is the location of the factory. There are many considerations involved in the solution of this question. The location of a factory has an important bearing upon the management and the general prosperity of the plant. One of the earliest influences at work in the selection of a factory site was available power. No longer human labor can be employed to move the powerful machinery of the factory; it is only by the generation of large units of power that the factory system is possible. In its early stages water was the only power that could be readily utilized. For this reason the first factories were grouped around waterfalls. No better illustration of this can be found than in the location of the factories of New England. In fact, it was the water-power that gave such a great impetus to her manufacturing industries, and which to-day furnishes the basis of the continued prosperity of this section. A new interest in water-power has been created by its utilization in the generation of electricity. The more recent movement is best shown by the conversion of Niagara Falls into electrical power for manufacturing and other purposes.

But, before the use of water-power for the generation of electricity for manufacturing purposes, the opening up of coal deposits led to the concentration of the manufacturing business near them. The rise of factories near Pittsburg and

in the Midland counties of England is doubtless due to the coal deposits and the early difficulty of transporting them to other places.

The development of our modern transportation systems made them a controlling consideration in the location of factories. It finally resolves itself in the main to a question of freight rates. From this point of view it is a question of the transportation of the raw material or the finished product, or both. Often the raw materials are heavy and bulky and the transportation rates correspondingly high. On the contrary, where the value of the raw materials is relatively small in proportion to the finished output, the transportation can be made more economically over longer distances. This is true of cutlery and steel factories. The location of paper and lumber mills on streams near the raw materials serves as an excellent illustration of how the bulk and weight of raw materials governs the selection of a factory site. The recent location of cotton mills in the South testifies to the force of this consideration.

In some lines of manufacturing nearness to the market is of more importance. This is particularly the case with small factories. The small factory cannot successfully compete with the larger ones, for the reason that the volume of business is important in securing rates and in sustaining a large and expensive selling organi-

zation. It is in the manufacture of staple commodities by small factories that nearness to the consumer is of more importance than close proximity to the raw material. It enables the manufacturer to keep in touch with his trade and to meet more carefully the demands of his market. Where the small manufacturer is located at some distance from the consumer, he is compelled to rely too much upon the jobber to find a market for his output.

The location of the factory with respect to raw materials and the market affects the organization of the factory in two ways. In the first place, it will determine to a considerable extent the character of the purchasing and sales departments, and, in the second place, the cost of transportation. We may take the sales department as an illustration. The location of the factory often determines whether the manufacturer is to organize a fully equipped sales department, or whether it is to be limited, relying upon jobbers and wholesalers to sell the output. If the manufacturer is doing a large volume of business, he is then in the position to organize his own distribution, and can consequently locate without reference to the consumer. An examination will show that this condition ultimately controls in the organization of the sales department.

Another example will suffice to illustrate the truth of this observation. The location of the

packing-houses near Chicago was largely due to the excellent systems of transportation, combined with its proximity to the live-stock belt of the West. But more recently the tendency has been to establish new factories near the feeding grounds of the West, at Kansas City, Topeka, and other points. It is found that it is more economical to transport the output of the packing-house long distances, than the live-stock. Again, the tendency to follow the consumer is well illustrated in the farm-implement business. The principal implement-manufacturing plants are located in the Middle West, in Ohio, Indiana, Illinois, and Wisconsin, but are to-day moving westward through the establishment of branch factories in the new agricultural regions of this country and Canada. The importance of transportation in determining the location of the factory is so obvious that only a mere reference to it is necessary. Larger factories require good terminal facilities and often two or more lines of transportation in order to secure favorable rates.

The most important consideration in determining the efficiency of the manufacturing business is the labor market. In its broadest sense it involves the general welfare of the employees; this is true especially of the larger factories. It is essential that the factory be able to command at all times efficient men in the labor and administrative departments. For this reason there are

certain advantages in locating a large factory in or near a large city. Especially is this vital to the problem of securing skilled labor and administrative help. A manufacturer must secure his skilled workmen by competing with factories doing a similar work. He desires men of experience. This experience must come from continued service in the factory itself, or from other factories. A constant supply of skilled labor must be available for the factory. The difficulty of securing this has been so great that many manufacturers have established apprenticeship instruction in connection with the regular factory work. In this way young unskilled persons are trained for the more skilled positions; the plan has proven satisfactory. Some manufacturers issue prospectuses calling attention to the favorable location of their factories.

There are certain influences outside of the factory of great importance in maintaining the efficiency of the plant. The laboring force must be content when off duty, or else inefficiency in the factory itself will result. The improvement of our modern cities in the way of parks, recreation grounds, public amusements, and of social life in general, opens up large inducements to keep the laborer in the large cities. It is generally conceded by managers that it is difficult to induce the employees in the administrative and skilled labor departments to remain in the employment

of factories which are located in places where these conditions are not found. The managers of our large factories appreciate the value of an attractive environment, and their employees are often induced by prizes to keep their home surroundings beautiful. Some factory managers provide club-rooms, cafés, libraries, and amusement halls for their workmen. These are considered good business investments, because they increase the efficiency of the laborer.

The employees generally prefer to remain at a point where there is a constant demand for employment without a change of residence. This carries great weight with the manufacturer in locating his plant. Where numerous factories are established we find that the laborers naturally gravitate to this point. On the other hand, some grave disadvantages are found in selecting a large city for a factory site. Land values are high, labor disturbances are frequent, and sympathetic strikes and risks are present in which all the factories are likely to be involved. The cost of labor is likely to be augmented under these circumstances.

In many cases one line of manufacturing business is closely dependent upon another. Certain preliminary processes must be gone through before the article is finally completed. In the steel trade, for instance, rough iron ore must be converted into preliminary products before it can

be used in the manufacture of machinery. This is equally true of a great many other manufacturing lines, and consequently it is often important that the factories be located near each other in order that they may do their work economically.

It is also found that factories doing a similar kind of business generally tend to segregate. No better illustration of this fact can be cited than the growth of the wagon and implement-manufacturing business at South Bend, Indiana. These factories are devoted largely to the manufacture of vehicles and plows. The city became a market for these commodities, and the smaller plants secured a certain advantage in publicity by coming to a market already established and widely known. Moline, Illinois, is similarly known as an agricultural implement manufacturing center. At Gary, Indiana, many small plants are locating near the steel plant of this place.

It is impossible to determine the relative importance of these considerations in locating a factory; but the manufacturer must weigh them carefully, for they determine in a definite way the success of the business. It may be impossible to combine all of these requirements in one site, but their influence upon the prosperity of the business is felt. Manufacturing concerns attempt to supply the deficiencies by other means. No better instance of an attempt to supply some of these

deficiencies can be cited than the town of Pullman, or the work undertaken by the National Cash Register Company at Dayton, Ohio. These concerns make special efforts to provide favorable living conditions for their employees.

We have already noted that the manufacturing business is divided into the factory and the commercial or office organization. While the two are usually united under one supervision and management, they may be altogether distinct, and even located in different places. For instance, where a large manufacturing business combines several factories, it is customary to establish a central office at some convenient point for their general supervision. Particularly is this true when the organization undertakes the marketing of the output. In this case the office is located at some important market with its branch offices at secondary distributing points.

In view of this general tendency, we shall consider the office only in its relation to the factory, and reserve the larger commercial phases for the discussion of the organization of distribution. The character of the office organization will depend upon the extent to which the factory engages in the purchase of its raw materials and the sale of its output. If the jobber and wholesaler perform this service, the office organization will be limited to the care of those matters of immediate importance to the factory. In this age

of consolidation it is quite customary to manage several factories from one central office. It is only in a general way that the policy of each factory is affected and controlled from the central office. Each factory is usually treated as a separate and distinct organization, and held accountable to the central office for definite results. It is not altogether easy to determine the exact scope of the office and factory organization. The factory must be taken as a starting-point, and is the main factor in determining the actual nature of the office organization.

Before discussing the factory organization, there are certain general matters that should be presented. Almost invariably manufacturing concerns are organized as corporations, and consequently the initial authorities are the same as found connected with any corporation, irrespective of the kind of business. These consist of a board of directors, president, secretary and treasurer. But when the business becomes large and complicated, additional authorities are created to represent the stockholders, and especially the directors, in shaping the details of the business policy. In some cases these consist of an executive committee, but with larger concerns other committees of supervision are frequently created. For instance, an advisory committee is established to represent the executive committee. Some of the very large firms have several com-

mittees to supervise special branches of the business, such as finance, sales, purchasing, improvement, etc. These sub-committees are not always permanent, but the executive and advisory committees are permanent, and are selected by the directors from their own numbers.

Closely related to the executive committee are the advisory committee, auditor, and general manager. These are appointed by the executive committee. Since the general manager represents these various authorities in the administration of the office and the factory, this is the proper place to present his powers and duties. In all instances the president represents the board of directors acting with the committees which are appointed by the board. To his duties as president are frequently added those of the general manager. In fact, in the larger corporations, the president is almost invariably the general manager. However, the duties of the president and general manager may be discharged by different individuals.

The general manager should be familiar with the technical phases of the business, as well as its commercial aspects. Above all, he must be a strict disciplinarian, and possess the judgment and tact of a successful organizer. His work is one of peculiar difficulty. Under his direction come the heads of the various departments of the office, as well as those of the factory. He is

the pivot of the whole business; he looks to the directors and their committees for the approval of his policy, and to the managers of the various departments to carry it out. Because of his intimate knowledge of the business he largely determines the policy of the firm.

The duties of the general manager are those of supervision and direction. A successful manager does not attempt to do the work of his subordinates, but reserves his talents for the larger problems of administration. For this reason the general manager's ability to select capable subordinates largely determines the success of the business. He receives the reports of the various departments in summarized form, and in this way keeps in touch with the minutest details of the business. The manager's authority is usually limited in two ways. In the first place, with the larger firms, he works under the immediate direction of the advisory, or the executive committees, and, in the second place, he is limited in his expenditures. His general powers pertain to finances, contract sales, banking facilities, wages, insurance, office and factory systems, advertising —in short, all of those matters that are essential to the well-organized and well-managed business. The manager's authority extends both to the factory and office.

We may now turn to the organization of the factory. The principles of factory organization

enable a great expansion and elaboration of detail. The arrangement and size of the factory buildings will be determined by the kind of manufacturing, and the volume of the business. This arrangement, both as to buildings and division of space, should permit the product, or parts of the product, to move progressively toward the finished stores room without any reversal of direction and with the least expenditure of power and time. There must be system in the arrangement of floors and wise planning and location of the departments for light, sanitation, and economic handling of each piece, for all these things secure the highest efficiency.

These considerations suggest the division of the factory into departments. The number of these will depend upon the number of processes into which the manufacture of a given product can be naturally and economically divided. There are two lines of division in every factory. In the first place, there is the separation into departments; and, in the second place, with the increasing volume of business, there is the further division of each department into sections. It is this that gives to the factory its unique position as a type of organization. As an illustration of this general truth, we may refer to the manufacture of machine-made shoes. In order to be able to use machinery, the shoes must pass through many stages of manufacture for the reason that

each machine must repeat its own work. Each step requires special machinery, special workmen, and special supervision, so that each department is made by the grouping of machinery and workmen around each definite process. This becomes fundamental to the economy of every manufacturing establishment. As a rule, the number of processes will be determined by the degree to which machinery can be used, and the size of each department will depend upon the amount of business which the factory is doing. The more general departments of the factory are the superintendent's office, drawings, patterns, experimental and models, tool-rooms, receiving-room, finished stores, rough stores, foundry, assembling and erecting, engineering, painting, power, and fuel. These departments multiply and subdivide rapidly with the growth of the plant; the machine shop in particular may be subdivided as the result of specialization in machinery and workmanship. In this way the work is thoroughly systematized. Everything is graded and subordinated from the work of the manager down to that of the least employee.

In charge of the factory organization is the superintendent, and upon him rests the responsibility for its efficiency. The superintendent works under the general manager of the whole business. He should possess not only a technical knowledge of the business, but also a knowledge

of men. All orders for factory work are issued through him to the various departments. He must know the condition of each branch of the business, its wants, and capabilities. He must be able to follow the output through its various stages, and give information with reference to the filling of orders. And especially must he be a judge of materials. This implies a system of reports from the foreman in charge of the various branches of the factory. The superintendent becomes, therefore, a very important element in the success and efficiency of the factory. Through the superintendent requisitions for materials for production, as well as for machinery and supplies, are made, and he is likewise responsible for the allotment of work and the execution of orders. In other words, his business is production and its delivery on contract time.

Immediately below the superintendent are the various foremen in charge of the different departments. In some instances the departments are grouped and placed under the assistant superintendents who hold supervision over the foremen. The latter are placed over such departments as the foundry, raw material store-room, the finished stores room, the drafting-room, and similar divisions of the organization. Each foreman is held responsible for his department, and reports its condition to the superintendent, who in turn summarizes these reports for the general man-

ager. The work of the foremen is largely, however, confined to the selection, supervision, and discipline of his labor force.

The next step in the organization relates to the individual workmen. The superintendent of the factory must determine what policy he is to pursue in regard to labor. He must determine whether he will deal with the individual laborer, or with labor unions. From the point of view of the manager the primary consideration is factory efficiency. If in his opinion organized labor renders the factory more efficient and increases the quality and quantity of the output, without proportionate increase in cost, he will not oppose the labor organizations for business reasons.

But, on the contrary, if organized labor introduces regulations and restrictions relating to the labor day, wages, and other expensive innovations, which often, from the point of view of the manufacturer, interfere with the efficiency and economy of the plant, he will desire to deal with the individual laborer. It is largely for this reason that many managers submit with reluctance to the introduction of organized labor into the factory. The feeling has been dominant that it tends to render the factory organization subservient to the wishes and demands of an organization which does not always have in view the efficiency of the plant. This phase of factory

organization will be discussed more fully in connection with cost-keeping.

It very frequently happens that the interest of the factory requires the exclusion of the public, not only because its free admission would interfere with the work of the plant, but also for the reason that often the manufacturing processes are secret, and must be guarded. The time of the men belongs to the factory, and for this reason, as well as to prevent fire, it is often guarded by special policemen and door-keepers.

But perhaps the most essential service of the gate-keeper is to watch over workmen. For this reason at certain points are stationed persons or special devices to record the ingoing and outgoing workmen. Many devices have been invented to aid in this work. In most of the factories some special machine is placed at a convenient point whereby each workman can register his arrival and departure; in other instances the check system is employed. This close watch over workmen is based upon the idea that no individual is independent of the factory, but that each workman must be at his place on time, and leave at the regularly appointed hour. These records are also used in making up the wage-slip of each workman in those factories where the compensation is by the day or by the hour.

One of the important departments of the factory is the raw material department. The man-

ager of this department stands in close relationship to the purchasing department and the superintendent of the factory. For this reason, in some cases, the raw material department is considered as a part of the general office organization, while in other cases it is considered as a part of the factory organization. In the larger factories it is under a special manager or clerk. He may not be empowered to purchase stock, but in this case must keep the purchasing department fully informed concerning the factory needs. He is closely identified with the factory and office, and might be treated as a part of either organization.

After orders are received from the general manager for production, the shop superintendent makes requisition upon the clerk of the storeroom for materials. If designs are required, they are furnished by the drafting department. The shop superintendent then issues orders to each foreman for the production of a given number of parts in his department. With the preliminary steps completed, the manufacturing processes are gone through with, and the parts are passed to the assembling and erecting room and finally to the finishing room, where they await the order of the shipping department. The clerk of the finished stores room keeps a record of the output of the factory; a careful system is necessary for this purpose. All orders for shipment come from the general office to the finished

stores room, and are then transferred to the shipping department.

It is the business of the shipping department to assemble the parts for shipment, and to make out a bill of lading to be forwarded to the buyer and recorded with the office. In the larger plants it is the duty of the shipping-clerk to know transportation rates and other conditions pertaining to the shipment of goods. The jurisdiction of the factory organization begins with the materials received from the raw material store-room, and ceases when these are turned over as finished products to the finished stores department. We have considered the raw materials and finished stores departments as part of the factory organization, but only in their narrowest sense. But they must be considered as closely related rather than forming an integral part. The factory operates under orders from the general manager only. Some of the factory departments are productive while others are non-productive. The former are engaged in actual manufacturing, while the latter are engaged primarily in administrative work and in the preparation of drawings.

It is very difficult to draw the line accurately between the factory and office organization. The practise is divergent. There is, however, everywhere recognized a distinction between the manufacturing and commercial phases of the business, which has resulted in the grouping of

the various departments into factory and office organizations. Naturally, a number of departments might, in practise at least, be united with either of the broad divisions. But the purely commercial transactions, such as buying, selling, advertising, etc., are often carried on at some point far distant from the factory. In this case these departments, closely related to the factory, become a part of its organization.

VI

COMMERCIAL ORGANIZATION

In the last chapter the distinction between the factory and its commercial or office organization was indicated. When located at the factory, the office is situated either in the main factory building or in a building near it. It contains the space for the office of president, board of directors, general manager, treasury, auditing, legal, correspondence, sales, publicity, purchasing, and other minor departments. The number of these departments will depend upon the extent of the business.

The tendency to locate the central office at some important business center is more pronounced to-day than formerly, and is the result of the consolidation which is going on in all lines of the manufacturing business. When many plants are brought under the same management, it is often found convenient and economical to establish at some business center, like New York City or Chicago, a central office for the management of the general affairs of the business, and at the same time to retain at each factory an office for the direction of the local affairs. This is true particularly of those firms that give large atten-

tion to the purchase of their supplies, and to the sale of their output. For instance, there is the American Tobacco Company, with its central office in New York City, controlling from there its buying agents in every leaf market, directing its factories scattered over the East and the South.

The commercial organization of manufacturing is not fixed by such rigid conditions as control the factory organization. The organization of a factory is fixed by mechanical processes, while the commercial processes are more elastic. It is concerned largely with human relations, and the principles involved are of such universal application that the form of the commercial organization is in every essential similar in all lines of manufacturing. The same departments are found either separate or consolidated. This obviously is the result of similar universal functions which must be assumed by the office organization, and which are capable of being divided and administered separately. An examination of the commercial organization of any manufacturing business will reveal the existence of similar departments.

One of the most fundamental principles governing the office organization is the division of labor. As the business grows, the duties increase in importance and in scope, and result in the creation of new departments under separate arrangements. The object of this specialization

is not only to secure administrative economy, but also to fix and enforce responsibility. The necessity of a sharp definition of duties and a gradation of responsibility compels the organization of the administrative force into departments with their various subdivisions. This responsibility begins with the board of directors and special committee, and passes on through the general manager to the clerks of the office and to the workmen of the factory.

The presence of these departments indicates the natural division of the various branches of the service. A department is the subdivision of the office, resulting from the grouping of closely related duties, which are necessary to complete certain transactions. For instance, we find in most offices an accounting department; in this department will be grouped those persons who are engaged in keeping the accounts of the firm. Likewise, in the advertising department, will be grouped those clerks who handle all matters pertaining to the publicity of the business.

Before taking up the organization of the office, attention should be called to a practise which is obvious and necessary in the economy of the administration. The duties of the commercial organization naturally fall into two groups: first, those of a general character which relate to general supervision and which must be attended to by the directing officers of the business; and,

second, those duties of a clerical nature, which are attended to by the individual departments, and which are not referred to the general office except in the form of reports. It is upon this distinction, which is natural and obvious, that the commercial organization assumes a twofold character. For the administration of the general affairs of the business the office of the general manager is established, and for the direction of clerical duties the various departments are created.

In the foregoing chapter we considered the office of the general manager, who directs and supervises the general affairs of the business. In addition to this general supervision and direction, we find the following special departments: viz., the assistant manager's office, accounting, orders, purchasing, sales, and stenographic.

Over each department of the office organization is placed a manager, who is the personal representative of the general or assistant manager in the supervision of his department. He is charged with its organization and the selection of clerks, is required to make frequent reports, and is often called in for personal consultation. The purpose of this arrangement of department heads is to surround the general manager with skilled administrators. It also frees the general manager from the burden of details.

Frequently the policy prevails of assigning to the secretary of the board of directors additional

duties. In some instances he is made custodian of the finances of the firm. Among all the departments the treasury, with the exception of the office of general manager, probably, is the most important. This department is the custodian of the funds of the business. In some cases the various branches of the financial administration are grouped under a department of accounts. Where this plan is followed, the treasurer is usually the head of the department. Its divisions are generally the treasury, cashier, bookkeeping, accounting, collecting, and pay rolls; its function is to supervise the manner and method of handling the purely financial matters.

In most instances the work of the treasurer is perfunctory, and is confined to receiving and paying out moneys upon proper vouchers, and in keeping a proper record of these transactions. The cashier passes upon the bills, drafts, etc., and his duties are similar to those of the cashier of a bank. It is the duty of the accountant—or, as he is sometimes designated, the head bookkeeper—to develop the systems of bookkeeping and to pass upon all the matters arising in this branch of the office. In the office of the larger manufacturing plants, in addition to the department of accounts, a separate department of audits is maintained. It is the duty of this department to check up all phases of the business in order to discover the mistakes, leaks, and losses. In the smaller plants

this department is frequently combined with the accounting department. This side of the office organization is receiving more attention than formerly.

Every manufacturing concern has need of legal advice. The smaller firms often combine the legal with the collection department, but in the larger ones it has an independent existence. It is the duty of this department to guard the legal rights of the firm, and draw up all contracts and other legal papers in conformity to the laws of the various States in which the firm does business. To it is turned over those claims where legal process is necessary for collection. In addition to this purely legal function, the department usually represents the form on those occasions where extended arguments are necessary.

In close connection with the legal department is the credit and collection department, although the latter conducts its work independently, except where legal processes are necessary in the collection of accounts. The larger manufacturing plants have special collection departments. Credits and collections are so important in all lines of business that a special chapter will be given to this subject. In this place we shall not discuss the organization of credits and collections, but rather point out the general relationship which they sustain to the manufacturing business. Every manufacturing concern makes its own

settlements and collections where possible. These are usually made from the central office. Some plants have their special collectors, who make the rounds of their customers and adjust accounts with them, and in some instances road-men are employed as collectors. When road-men are employed they are held responsible for the extension of time to buyers whose credit is bad. Hence they are personally anxious to avoid bad sales. Where the firm sells to jobbers, the collection becomes somewhat easier, because the financial standing of the jobbing firm can be readily ascertained. On the other hand, where the business is carried on with retailers through the sales department, the extension of credits and the enforcement of collections become more complicated, and the liability of loss much greater. It is obvious that the manager of this department must be fully familiar with the business standing of all firms and persons who are likely to desire an extension of credit. The department must be fully equipped with the aids of modern business for gathering and tabulating the information necessary to form correct judgments as to the financial standing of customers.

An important fact to be kept in mind is the dependence of the credit department of all business firms on such mercantile institutions as Dun and Bradstreet. The manufacturing business is no exception. The credit department of the

manufacturing plant has its own sources of information as to the financial standing of its customers; still, it must rely to a great extent upon the information furnished by these larger credit agencies.

Naturally, the work of the office involves a large amount of correspondence, both of a special and general character. The special correspondence is conducted by the general manager, and the heads of the various departments, while the general correspondence is carried on by a department created for that purpose. This department thus looks after all correspondence that does not require special attention. In this way the stenographic work is kept in order and may be easily consulted at any time. Special language training is often required for correspondence work, especially if the firm does an export business.

Since the character and cost of the raw materials so largely determine the character and cost of the factory output, the purchasing department of the factory is one of the most important of the office organization. Its work, however, is greatly facilitated, because, in the natural order of business, the sales department of those firms handling raw materials and factory supplies is on the alert to find a market for them. For this reason the work of the purchasing department of a factory is critical. Where the factory requires raw materials in great quantities, the manage-

ments have sought to control the source of these materials through ownership. The United States Steel Corporation owns extensive ore deposits, and the Standard Oil Company owns extensive oil fields. But in the case of the smaller factories the materials and supplies must be secured in the market. In this case the purchasing department has important work to do. In the place of the rudimentary department of the earlier or small factories, we now often find a complex machinery, with its agents in every important market. The purchasing of materials and supplies and the sale of the output of the factory brings us into the field of distribution, and a more comprehensive treatment of this subject will be reserved for another place.

Each factory maintains a purchasing department. Where several factories operate under one central management, the purchasing department is a part of the general office, and each individual factory makes requisition upon it for supplies. It is the business of the department to keep in touch with the sources of supply and the conditions of the market. In order to purchase intelligently and economically, there must be a thorough knowledge of the factory output, as well as of the market. If the factory is doing a standard business, the purchasing of materials is not so difficult as in the case of manufacturing on special orders. Whenever it is possible, the

raw materials are secured in large quantities on contract. These contracts are usually drawn for a definite period. The purchasing department is acquainted with the sources of supply and conditions of the market through catalogues and list prices. In most cases the contracts are made after competitive bidding. It is the duty of this department to keep the store-rooms ready to meet all the demands of the factory in reference to machinery, supplies, merchandise, and materials.

The delivery of raw materials is an important element in the economy of the factory. In order to avoid insurance upon large quantities of raw materials in the warehouse, it is customary to draw all contracts for delivery at specified intervals, or upon sufficient notice. For this reason the jobber and commission broker are largely employed by manufacturing plants where the system of direct buying is not followed. This is so especially in the purchasing of cotton, cereals, wool, etc., for manufacturing purposes. However, in the case of iron and other metals, the policy is to control the source of supply. Where the factory uses materials after they have passed through certain stages of manufacturing, it is customary to contract with the factory. In the purchase of supplies two methods may be followed—the one, to ask bids, and the other to go into the open market and buy in competition with other firms.

The sales department of the commercial organization is more necessary than that of the purchasing department. The factory must sell its output. It must find a market and in many instances business must be created. As in the case of the purchasing department, the sales department may be rudimentary. It may be the policy of the factory to sell to the jobber, or to sell its entire output, or a large portion of it, under contract. This policy was formerly followed by most factories, and is followed to-day in many instances by the smaller ones. But more recently the tendency has been for the larger manufacturing plants to adopt the policy of direct selling in so far as it is economical. The primary reason for this change is the close competition in the market, which compels the factory to give more attention to the sale of its output, and also because of the larger use made of publicity in creating a demand.

Whatever policy may be pursued, the factory maintains a sales department. This department may have very little work to do, or it may be elaborately developed into numerous branch offices, and may even enter the business of retailing. As a rule, the office adopts one of two policies, or a modification of these. It may organize its sales department and establish branch offices, and put upon the road men to search out the retailer and the customer; or it may depend

upon the jobber and wholesaler to find a market for the output. The adoption of the one or the other of these methods will depend largely upon the volume of the output and the character of the demand. Where the goods must be pushed, the system of direct sales seems to be greatly in favor. The expense of maintaining an extensive sales system is large, and cannot be met unless the volume of the sales is materially increased, or the margin of saving through the elimination of the middleman is sufficient to meet it. Where the factory does its business upon special orders, the sales department is only nominal. It solicits business. Trade is sought and no output is extensively sold. The head of the sales department must be in touch with the factory; he must be familiar with the condition of the warehouse and the trade prospects. Whenever uncertainty prevails as to credit, he must rely upon the advice of the credit department.

Operating in close connection with the sales and purchasing departments is the estimating department. Those factories doing a large business employ a corps of persons to prepare estimates of the prices of raw materials, and also of the output of the factory. These estimates of prices are based upon the data presented by the cost-keeping department. It is only after the cost of manufacturing has been ascertained that the estimating division can determine at what

price the output can be sold, as well as the prices which can be paid for raw materials. While in a general way it is true that the price of raw materials must be determined in the open market, and the factory output sold in competition, still, the work of the estimating department will often enable a selection of materials which will keep down the total costs. It also indicates to the sales department the minimum price which can be taken for the output of the factory. The work of the estimating department is based upon the system of cost-finding employed by the factory. The estimating clerk keeps a file of catalogues and price-lists of firms dealing in the supplies needed by the factory. The main function of this department is to determine the price at which the output of the factory can be sold. This work is exclusive and secret, and the information is carefully guarded, even from other departments.

There still remains one more important department for a brief consideration. In this age of publicity every manufacturing firm seeks to make itself as independent as possible of the jobber and retailer. In order to do so, it must interest the customers in its wares. In order to create this demand, the factory supports an advertising department which has general supervision over all the publicity of the firm's business. It determines its advertising policy independently or in connection with regular advertising agencies. It

selects the various publications through which the firm is to make known to the public the character of its output.

As suggested, the advertising department may take entire charge of the publicity, or it may turn it over to a regular advertising agency. In either case the department prepares advertising material, and keeps general supervision over periodicals from which it buys advertising space. While many of the firms virtually take charge of their own advertising, still, the rise of advertising agencies in recent years has curtailed somewhat the work of the advertising department of the factory. These agencies have so organized the field as to make it advisable in many instances to turn over the advertising campaigns to them. When this is done, however, the advertising policy is developed in the light of the information furnished by the advertising department of the factory. The board of directors usually set aside a certain sum of money to be devoted to publicity, and it is the business of the advertising manager to use this money in the most effective way. A fuller consideration of this subject will be found in the chapter on advertising.

Our object has been to point out the function of the various departments of the office organization and to show their relationship to each other. It has also been our purpose to indicate some of the forces which determine the extent and char-

acter of this organization. Their function is to keep the factory going, to furnish it with supplies and sell its output, and to take charge of the administrative work. We have already seen that much work of the office lies within the field of distribution, and for this reason it will be taken up in its proper place.

VII

FACTORY COST-KEEPING

In recent years great attention has been given to the subject of cost-keeping in all lines of business. For many reasons the cost of service, or of commodities must be known as a basis of intelligent selling. But while it is true that business men are everywhere more alert in ascertaining costs as a basis of selling, still, it is especially the case with manufacturing. For this reason we have chosen to discuss the subject in connection with the organization of the manufacturing business. We should not, however, lose sight of the fact that essentially the same principles apply to all business undertakings.

In some lines of business the margin between the cost and selling price is so great that little attention need be given cost-keeping. However, in other lines competition has lowered the selling price, so that, without an accurate system of cost-keeping, unsuspected and unknown losses often occur. In the earlier days of manufacturing the margin between the cost and selling-price was obviously so wide that little or no attention was necessary to prevent losses.

The history of commerce in the United States

shows its development under conditions of large consumption with high prices. Raw materials were cheap and accessible. With the demand for increased production capital was gradually invested, with the result that in many lines of manufacturing competition lowered the margin of profit. This situation forced the trust movement, and in the latter case induced over-capitalization. Consequently the trust, on the one hand, and the competitive plants, on the other hand, have been compelled to give greater attention to the subject of cost-keeping as the basis of selling and business economy.

Many instances might be cited where failures have resulted because little attention had been given to the cost of production and distribution. Improper charges for depreciation, interest, materials, labor, and various other items afforded opportunity for serious mistakes in ascertaining accurately the final costs. In prosperous times, when the demand for the factory output is large and prices high, the necessity for a system of cost-finding is not so apparent, but when the management is forced through competition to a low margin of profit, and in some cases to actual temporary losses, it is necessary to know the costs and to develop some plan for their distribution.

When an inquiry comes into the office asking for a tender of prices, it is necessary for the estimating department to know the cost of producing

that commodity. Competition with other firms doing a similar line of business will determine the selling-price until it approaches the cost of production. The factory managers must keep constantly before them the relationship between these two sets of prices. Competitive prices do not form an accurate guide in fixing the selling-price, because the conditions of operation and management vary so widely. Two factories selling the same output and at the same price may mean profit for one and loss for the other. For this reason the firm with a small output is often at a disadvantage in competition with one with a large output in this day of quantity selling.

A good system of cost-keeping is generally recognized as an essential feature of successful factory organization. It enables the manager to know, not only the results of competition, but likewise the profits of prosperous times, and the losses of disastrous ones. It has much to do with the success or failure of his business. As a guide to the management, its value cannot be overestimated. Not only have factories been closed down because a faulty system of cost-finding failed to reveal losses, but frequently, by reason of a proper cost system, valuable machinery has been destroyed because it has been shown that more economic methods and machinery could be utilized. These and many other facts can only be brought out through a proper system of cost-

finding. Under many circumstances the selling-price of the factory output is largely guesswork, and is only admissible where a large margin of profit exists; but it fails to make known the time when that margin is destroyed, and the business becomes a losing one. A correct system of cost-keeping will bring these facts fully before the manager, and will enable him to shape his business policy in harmony with them.

A system of cost-keeping is the statistical demonstration of the effectiveness of the business. In manufacturing it is an outgrowth of the plant itself. In the early days of manufacturing a system of cost-keeping was unnecessary for practical purposes. Where the price of the output is not seriously menaced through competition, a system of cost-keeping may be rudimentary, and primarily as a guide to improved management. Factory organization was simple, but to-day it has become so complicated, that something more than supervision is required. It is still claimed by some factory managers that detailed cost-keeping is useless, and that all necessary facts can be secured from the foreman; but the prevailing opinion of to-day is that factory management becomes safer with an effective system of cost-finding.

The main features of factory cost-keeping are applicable to all manufacturing concerns. They may, however, differ in detail. Any system of

cost-keeping will depend upon the kind of information sought. While different systems and methods may be employed in determining the cost, the same elements must be considered in all cases. A different grouping of departments and divisions gives each manufacturing plant an individuality of its own, and makes necessary a special treatment of cost details for each factory.

In determining costs, two classes of items must be considered: first, those of a fluctuating character, such as labor, materials, supervision, etc.; and, second, those of a more permanent character, such as charges for depreciation of machinery, buildings, insurance, interest, etc. The relationship which these two groups of cost items sustain to each other will depend, of course, upon the kind of manufacturing. In fact, all the elements vary in detail with the nature and volume of the business. A factory which buys only one class of raw materials and manufactures only one article can use a simpler system of cost-keeping than one which manufactures a varied output.

For the purpose of determining the nature of cost-keeping it is customary to divide factories into two classes: first, those producing individual uniform commodities, such as boots, hats, machinery, etc.; second, those producing a commodity which is not a unit in itself, but is sold by weight or measure. Such well-known commodities as wire, paper, textiles, fall within this

class. In the first instance the items of cost are more detailed and must be apportioned among the different articles, while in the second case the costs may be readily ascertained and apportioned for definite periods of time.

ELEMENTS OF COST

Selling Price

FINAL OR TOTAL COST		PROFIT
Factory Cost	Commercial Cost	
Prime Cost	Office Expenses	
Material	Salesmen	
Direct Labor	Patents	
Burden	Legal Services	
Plant and Buildings	Advertising	
Rent	Traveling	
Depreciation	Upkeep	
Insurance	Bad Credit Reserve	
Light, Power and Heat		
Taxes		
Upkeep		
Machinery		
Indirect Expenses of Production		
Indirect Labor		
Factory Supplies		
Expense Tools		
All other Factory Expenses		

Before taking up the various systems of cost-keeping, it will be useful to define briefly the terms most generally used. "Prime or factory cost" means the cost of labor, plus the cost of material, plus all indirect expenses, or the burden chargeable solely to the account of the job or piece. These latter items are wages, upkeep of

plant, light, power, rent, taxes, etc. "Total or final cost" means the entire cost of a piece or job, and is composed of the prime cost plus its proper proportion of the selling or commercial expense account or estimated charges. This latter includes such items as salaries, upkeep of office, advertising, traveling expenses, legal service, etc. Total costs are composed of these items, together with factory costs, which are again divided into prime costs and the burden. The latter is a subject of great controversy, especially its apportionment.

The most difficult cost to determine is "factory cost" for the reason that it includes such variable elements as wages, materials, and the burden. It is, however, the most important phase of cost, because the estimate of prices is usually based upon factory cost. For the total cost is easily determined by adding to the "factory cost" a certain fixed percentage of the expense of distribution and administration, generally known as selling expense. The most important and constant items of the commercial expense account are salaries of office force, salesmen and advertising. In fact, the commercial expense account includes all items which are not primarily considered in factory costs.

The total or final cost of a given commodity is not always easily obtained, because of the fluctuating items which it includes, and, second,

the difficulty of distributing these items among the products of the factory. Obviously, different notions and practises prevail in keeping the various items of cost. In some quarters it is contended that only a very general notion of expense can be ascertained under any system, and that this will suffice to guide in fixing the selling price of the output, and that any attempt to reach the details of cost will be cumbersome, expensive, and inadequate. This is certainly the case with some systems, for they fail to secure accurately the costs.

It is generally agreed that costs fall into two groups. The first is usually designated as factory cost, and the second commercial cost. The factory costs or productive expenses fall into three divisions: first, the cost of raw materials; second, the cost of productive labor. These two are also known as prime costs. And, third, the indirect expense of production, or the burden. This latter class is made up of a number of items, such as wages of superintendents, foremen, and factory clerks, and expenses of the factory plant and buildings, such as light, rent, insurance, taxes, depreciation, and extension. These items are sometimes considered as a part of the general expense account for the reason that a certain percentage is generally added to the factory cost of the commodity. They are generally reckoned upon a percentage basis, and are added at the

end of a stated period, or to the cost of a given piece or job.

We will now take up the elements of factory cost in order to point out some of the methods employed in ascertaining them. The first item that appears upon the cost card is for raw materials. As soon as the requisition is made upon the raw material store-room the cost is entered upon that card, and charged against the factory. This part of cost-keeping is simple for the reason that some definite value can be assigned to the raw material for each job. Whatever system of record is used this cost appears first and in definite form. Some difficulties, however, may be met. In some instances values increase very rapidly during the process of manufacture, while in other cases the margin of increase is comparatively small. Consequently in some instances the cost of raw materials is very important, while in other instances of comparatively little importance. In some lines of manufacturing this item of cost can be fixed more definitely than in other lines. The cost of material includes not only its purchase price, but also such items as storage, freight, and clerical expense. It is sometimes customary to fix the cost of material by averaging the cost over a series of years instead of basing it upon the market price at a particular time. This makes it a constant element. In some instances 1% to

5% is added against the job for errors or excessive charges.

The second and most important item of factory expense is labor. By labor we mean the wages paid to the workmen and foremen directly engaged upon the manufacture of the commodity. A great many difficulties arise in the apportionment of labor, although in the aggregate it is easy to determine. There are two elements involved in keeping labor cost. The first is the time element, and, second, the labor skill. The time element must be taken as a basis, while the variations of expense appear in the gradations of skill required in the different departments of the factory. It is very difficult to measure by any standard which is accurate and just, and it is not easy to ascertain the quantity of labor used on a given commodity. If the laborers were equal in skill, some just standard could be devised. Even if the factory management desires to develop and reward skill, it is often made difficult because labor organizations are opposed to too much individualism in compensation. The management seeks efficiency, and should form its schedule of wages so that a constant stimulus for larger effort on the part of labor will be constantly present. Efficiency is measured in terms of the quantity and quality of the output.

As a result of these inequalities, the employer and laborer are struggling over the wage prob-

lem in all lines of industry—a struggle which gives to the subject a large public interest. The essentials of the controversy are well illustrated in manufacturing. The manufacturer desires naturally to secure the largest labor efficiency with the least expenditure of time and wages. The laborer, on the contrary, desires to get the largest remuneration with the least expenditure of time and energy. The meeting of these two interests in the attempt to adjust their differences has given rise to several wage systems designed to extend additional inducements for extra efforts. Labor unions have also come into existence to protect the workmen against arbitrary and unfair treatment by the employer.

A brief summary of the more important methods of compensating factory labor may throw some light upon the keeping of factory costs. We find as a rule two classes of workmen in a factory. One is the productive, or direct laborer, who is engaged directly upon producing an article in hand, and whose individual efforts enter directly into value of the commodity; the other is the non-productive or indirect laborer, who is engaged in auxiliary work necessary to produce the article, such as the preparation of plans and specifications, keeping time, supervision, etc. The usual method of compensation for the second class is that of a salary based upon time and importance of the position. They are usually

paid by the day, month, or year. These items of cost are more readily determined and distributed, because they are more definite and less fluctuating. The distribution is usually made upon a percentage basis, and is charged as a part of the burden and not as a part of the prime cost.

On the other hand, the greatest difficulties arise in determining the compensation of the productive or direct labor. Probably the simplest form of compensation is that based upon some period of time, such as by the hour, or by the day. This form of compensation is not universally satisfactory for the reason that it is an average wage, and fails to make proper allowance for the different kinds of work, or the varying capacities of workmen. This system may have its advantages from the point of view of cost-finding, but it fails, however, in the fact that it discourages the more efficient laborer, and often remunerates unjustly the less efficient one, and results in the restriction of the output.

As a result of this difficulty modifications of the time method of compensation have been introduced. These are based upon the varying degrees of activity and skill possessed by individual laborers, and several methods have been evolved to meet these varying qualities. In most factories will be found a class of rough laborers whose employment by the day or by the hour is fairly satisfactory and just. But as we pass to the more

difficult processes, the wage system is usually adjusted so as to give encouragement to the skilled laborer. Unless provision is made for the individuality of the laborer the efficiency of some of the departments will be impaired. If the laborer knows that his compensation will not increase with increased activity and skill, he is likely to be satisfied with a fair effort only upon his part. Consequently wage plans must be devised which will allow for the capacity of the laborer to do rapid and skillful work.

The first step is to compensate the laborer for the work that he actually does. This is accomplished by basing the wage on the job or piece. In its pure form the laborer is free to work as he pleases, both as to rapidity, skill and time, but the factory must be viewed as a unit, and, especially where machinery is used, it is frequently impossible to permit one laborer to work overtime or more rapidly than is consistent with a standard, based upon the work of the factory as a whole. For this reason there are not many factories where the piece system can be used in its pure form, and while the plan has many strong features to commend it from the point of view of the laborer, it is as a rule incompatible with the factory system except in a modified form. Again, where labor organizations exist, this plan is not viewed with favor for the reason that they are dealing with labor groups, and do not unite with

the individual laborer. Too great a difference in compensation between workmen of the same class and doing the same kind of work is discouraged. Consequently a uniform system of compensation is sought which rewards the laborer in groups and in classes rather than as individuals.

However, the greatest objection to the piece system in its absolute form is the fact that it is incompatible with the factory system, whose labor force must generally operate as a unit. There is also a tendency for the laborer to discover the amount of work which will give him a maximum wage beyond which he does not exert himself. Again, the piece-work plan is based upon speed tests which are frequently inaccurate. If the laborer exerts himself to full capacity, there inevitably comes a time when wage-cutting must follow, for the wage expense is so large an item of the selling price, which is constantly pushed downward.

In order to overcome this objection, and still permit each workman to enjoy in a measure the fruits of his own skill and continued effort, various combinations of the time and piece system have been worked out. The essential feature of these combinations is starting with a uniform wage for all laborers of a group, or those engaged upon similar kind of work, and then upon this basis establishing a sliding scale to reward those who possess special skill and dexterity and who

work overtime, where the factory operations permit it. There is thus fixed a living scale for all laborers, with the additional feature of providing an increased compensation for those who put forth special efforts or who display more than average skill. The piece system is thus employed as a modifying feature of a uniform fixed wage for all the laborers of the same class.

One of the well-known modifications is the premium plan, which fixes the price per piece and increases the compensation upon some scale determined by a fixed rate of speed. It is usually based upon an average standard rate per hour, with increased compensation when more rapid work is done. It urges the workman on at a more rapid pace, against a fixed standard; and yet it does not destroy the unity of the factory work by permitting one laborer to proceed too rapidly or to work overtime. The fixed compensation is based upon an average day's work for all the factory or a class of workmen, and the increased compensation provides a strong stimulus for increased effort without endangering the work of the factory as a unit. The system is extreme in its rewards and penalties, and for this reason is fairly satisfactory to the employer and skilled laborer.

Another modification of the piece system, and closely allied to the premium plan, is the bonus. This plan is based upon the separation of the work

of producing a piece or job into its elementary operations. In case the workman is unable to perform his work on a fixed time, he is paid by the day; but if completed on time, he receives his bonus for his efforts. Its feature is a minimum wage with the bonus for extra effort.

In recent years considerable attention has been given to the profit-sharing system, and it has been introduced in some factories. The object of this plan of compensation is to give each laborer a personal interest in the success of the factory. It is done either by turning over to the workman a certain percentage of the profits, or by assigning stock to him. Another plan of profit-sharing is known as the co-operative piece system. By this plan the labor cost is fixed for each piece, and the total gain divided among the workmen. This has met with some favor, because of the good effect which it seems to exert over the labor force as a whole.

We have presented these various plans for the purpose of calling attention to the effect of the wage system upon the efficiency of the factory, and as elements in cost-keeping, and not for the purpose of giving an exhaustive presentation of the subject. It will be observed that there exists in the factory possible conflicting interests in the constitution of the labor force. These are the interests of the manufacturers, the individual laborer, and labor unions. It is the purpose of

the former to secure the highest degree of labor efficiency in his factory with the least cost, but this does not mean it may not be economical to pay a high wage. Naturally, the laborer desires the largest compensation possible for the least expenditure of time and energy, but this also does not mean that the laborer can afford to grow lax and loose in his work. The two interests are identical and mutual, and in every successful factory labor troubles and strikes are not likely to occur when this view is taken.

The attitude of organized labor seems to be in the interests of average labor, and while it recognizes the efficiency of the different groups, it sees the danger of permitting too much individuality in the wage plan. In all probability the manufacturer would prefer to deal with the individual laborer, but the laborer is so helpless when standing alone that he is forced to protect himself by organization. Such an organization is likely to protect all laborers without regard to capacity and skill, except in so far as it recognizes these qualities by establishing classes, thus permitting a variation of wages. It must, however, be admitted that the trade unions develop labor efficiency by securing shorter hours, better working conditions, and improving the conditions of the working classes in general. Some manufacturers also take this view, and provide those things which promote the welfare of their la-

borers, and elevate the general tone of the factory environment. Manufacturers are coming to realize that labor unions, properly directed, possess great possibilities for good.

A third and final item of factory cost is the indirect expense of production, or the burden. This group is made up of several separate items, and forms an inexact element of cost. Among these are the wages of the superintendent and foreman who supervise the factory labor. Whatever system of compensation may be employed for ordinary labor, the expense of supervision is usually a definite quantity. This is true equally of other indirect costs of production. As shown before, those items include the expenses for the plant and other buildings, heating, power, operation, insurance, and taxes.

The method of distributing these various items of expense is the most important problem from the point of view of cost-keeping. The method will depend upon the desirability of fixing the cost for each manufactured article, or that of the output as a whole for a stated period. When the first method is employed, a given percentage is charged for the indirect expense for each article, which, together with the cost of material and labor, constitutes the factory cost. If it is the policy of the firm to keep the expenses of manufacturing for stated intervals, the indirect cost of production, or burden, is added for this period to

the other costs. This obviously does not require the same detailed work as in the first instance, for these costs are accumulated in definite sums of considerable amount.

There are three methods employed by manufacturers in apportioning the burden. The most usual one is the percentage plan, which is made upon the basis of values. The hourly plan is also used, which, as the term indicates, is an apportionment based upon a time period. Again, in some factories the machine-rate plan is used, which is an apportionment based upon the life and capacity of the machine. There are such serious objections urged against all of these plans that they are not wholly approved in practise.

Depreciation is determined upon some percentage basis, and obviously varies with the character of the buildings and the machinery employed. The depreciation for machinery is often very rapid and uncertain, and it frequently happens that new methods and processes of manufacture will compel the entire removal of machinery in good condition, or the building over of old machinery. The management must be alert in using up-to-date and efficient machinery, although changes often entail a great loss. Where the methods are well established, as in the case of the manufacture of watches, the depreciation of machinery is low.

The rate of depreciation for buildings will

obviously depend upon the location and materials. Ordinarily buildings depreciate quite rapidly. Buildings of brick and stone construction usually depreciate annually from one to two per cent., the foundry about four per cent., and wooden buildings from five to ten per cent. More frequently errors occur in the failure to estimate properly the rate of depreciation and other estimated charges; they are more often too low. And, again, not only does the character of the buildings determine the rate of depreciation, but it has also a strong bearing upon the cost of operating, heating, lighting, and insurance. Depreciation may be met in one of two ways: either by charging a fixed per cent. to the price of the output, or by creating a sinking fund. Depreciation may be calculated at the end of the year, or on the basis of a periodic or continuous valuation. Where the blanket plan of fixing the depreciation is not employed, a classification of the different items is made.

Taken together, the cost of raw materials, labor, and indirect expenses of production, or burden, constitute the factory cost of the finished output. Some of these items are definitely known, while others are quite difficult of accurate determination. No rule can be laid down of general application governing the determination of the indirect expense of production for the reason that these items fluctuate materially be-

cause of special conditions in different plants. It is the general practise to add a given percentage for each item.

We have already pointed out that the total or final cost of the output is determined by adding to the factory cost the cost of selling or distribution. The items composing this group are varied, and often quite large. While differences of opinion exist as to the classification of these items, it seems to be the general practise, however, to include under this head the salaries of directors and officers, the upkeep of the office, expenses of road-men, commissions, advertising, patents, legal service, and bad credit reserve. The difficulty of determining these expenses is probably not so great as in the case of factory or prime costs for the reason that many of them are definitely known.

The line between the factory cost and the commercial or selling expense is not drawn in the same way in all factories. In some instances the factory expense is confined to the cost of raw materials, labor, and those supplies necessary to keep the factory going; and the selling or administration expense includes such items as depreciation of plant, insurance, etc. The classification of these items is not, however, the most important question before the management, but it is whether all items have been properly considered in footing up the total cost of the output. It is essential

that all items of expense be charged against the proper account; the factory, for instance, should not be charged for expenses over which it has no control. This should be especially guarded against for the reason that each branch of work is entitled to know its own expenses. Classification is important only in so far as it will assist in developing an easy and accurate method of ascertaining the several items. It is usually necessary to go into far greater detail in determining these items than the limits of this chapter will permit. We have pointed out the principal items of cost which must be considered by all manufacturing concerns. The details vary when applied to specific plants.

With these essential elements of cost before us, we may consider the methods of fixing the selling price of the output. After the total cost is known, and the rate of profit determined upon, and added to the total cost, it constitutes the selling price. The selling price is based upon the cost of raw materials, labor, burden, selling expense, and the profit desired. It must not, however, be inferred that every manufacturing establishment follows this order in fixing the selling-price of its output; but, in times of close competition with a decreasing margin of profit, the firm possessing this carefully analyzed data will know when to cease cutting its prices, unless it desires for good reasons to sell below cost.

Accurate cost-keeping is not always practicable; still, substantially accurate results are possible. This accuracy depends upon the system of cost-keeping employed and the nature of the business.

One point of special bearing upon the selling-price should be noted at this time. Many firms, both manufacturing and mercantile, often make it known to the trade that they are doing their business on a certain percentage of profit. The declaration of dividends of various corporations further illustrate this. But it should be borne in mind that in many cases the profit bears no relation to actual costs of production, but often the dividends are distributed over watered stock; while in other cases insufficient charges have been written in for depreciation and other similar expenses.

Almost every factory uses some kind of a cost-keeping system. In many instances it is very crude, and does not attempt to go beyond the record of the general cost of the output for stated periods. The selling goes on to the end of a quarter, or the year, and an attempt is then made to figure out the profits or losses. This system does not enable the management to foresee disastrous losses until it is too late to correct them. This general system is permissible in a period of great demand and large prices, or where the factory is engaged in manufacturing a continuous product. Under these circumstances only the

most important items of expense are sought, and allowances are made for the minor items. But this is a system of guess-work, and fails to take into consideration the progressiveness of competitors, and the tendency everywhere to employ more efficient factory methods.

The business man is often at a loss to know why he should maintain an expensive system of cost-keeping, since cost has little to do with his selling-price, which is fixed by competition, or by custom. But a system of cost-keeping enables him to know when he can sell with profit and safety. It also enables him to discern the weak spots of his organization and to know the waste. Even when a competitive market does not exist, it is wise to conduct the business economically. The function of cost-keeping is to guard the manufacturer against losses and not alone to fix prices.

A more detailed system is wise and safe where competition tends to narrow the margin of profit. A system of cost-keeping is determined by the data desired, and the emphasis upon these items will be determined by the conditions in each factory. Some items may fall away, while others are greatly expanded. It may be desirable to know the cost from day to day, or for a stated period, or the cost of each particular piece of the total output, or the cost by departments and branches.

These differences in detail grow out of general considerations applicable to all factories, for each management is seeking essentially similar information for similar purposes. The selling-price must be determined, and economical and efficient methods of manufacture and administration must be maintained. For instance, a manager finds his margin threatened by falling prices due to strong competition with factories using better methods and possessing a more accurate knowledge of costs. He may recover his margin of profit in one of two ways. He may increase his output through increased effort without proportioned expenditure, or he may reduce his expenses of manufacturing and selling. It is the knowledge of costs in detail which will enable him to take the proper corrective steps.

Most of the early systems of cost-keeping were crudely developed with the growth of the business. Where the factory was small the costs were kept and grouped by the foreman. They were not as a rule devised by professional accountants, who now quite generally install such systems. The old systems were amorphous. They were not developed with the general principles of cost-keeping in mind, but rather with only factory conditions in view. Obviously a system of cost-keeping must be based upon general principles which grow out of an analysis of general facts based upon experience.

Generally the card system is used and for many reasons has become almost universal in business. It has made its way into the offices of all departments and lines of business because it means a definite knowledge concisely stated and classified. The most commonly employed system of cost-keeping seems to be the collective job-ticket system. By this system the cost of a single piece or job is recorded on one card. It usually begins with the factory order for materials, and follows the commodity through its stages of manufacture, and each item of expense is added in its proper order until the time of completion, when there is finally added its portion of the general expense account. In this way the total cost is finally secured. It is also capable of great modification, and for this reason is the favorite method of record for all lines of business. After the history of all the essential items of cost have been extended upon the card, it is then passed to the office, properly recorded and indexed under the supervision of the cost clerk, and becomes the basis of determining the selling price.

Various modifications of the collective job-ticket system are used, depending upon the nature of the manufacturing business. In some instances, instead of one card, two or more are employed, for the purpose of ascertaining particular costs. Sometimes the card follows the material to a certain stage, and is then super-

seded by another; it becomes a way-bill accompanying the article through its various stages of manufacture, and is employed to ascertain the efficiency of workmen or a department. For instance, the capacity of a machine is known to the foreman, and he is able to learn whether the workman has gotten out of it all that it is capable of doing.

The analysis of cost is the basis of action. It is the statistical summary of factory results. A great deal has been written on the subject in recent years, and many different systems have been devised; but we have only attempted to point out those features common to all factories without going into details, which vary widely in practise.

C.—ORGANIZATION OF DISTRIBUTIVE INDUSTRIES

VIII

EVOLUTION OF THE MARKET

In the preceding pages the leading features of the manufacturing business are outlined. Our next step leads to the organization of the market which lies between the producer and consumer. Agricultural surplus producing sections are often located far distant from the consuming population, and this is equally true of factories. For instance, the products of the Western grain belts must be moved to the East and to Europe, and the ores of the mine must be sent to distant factories and from thence to the consumer. These conditions materially increase the importance of the market.

Here is then a function distinct from production or manufacturing. The function of distribution[1] implies the existence of a separate organization, although it may under certain circumstances be assumed by those firms engaged in production and manufacturing. It is a matter

[1]Distribution is here used in the ordinary business sense, and is not employed, as the economists ordinarily use it, to refer to the distribution of income and property in thier various classes.

of common observation that in some communities the producer does his own marketing. Again, it is equally true that the manufacturer frequently sells his own output. But it is nevertheless apparent in these cases that to the primary purpose of those organizations is added the function of distribution or marketing. But, however, it is still true that in most instances the market is organized and conducted as a separate and distinct enterprise. The function of such organizations is to create a market for the producer, manufacturer, and consumer. A chain of markets is thus established and sustained by a special class of traders.

In the organization of the market the essential thing to note is the manner in which the seller and buyer meet to transact their business. From the earliest times markets have existed. The great markets or street fairs of the Free Cities of the Middle Ages are conspicuous landmarks of commerce, and some of these have even survived. The market halls of modern cities doubtless have their origin in these open periodic markets of earlier days.

In the course of time these markets were specialized. This doubtless grows out of the specialization of industry, which has gone rapidly forward in our modern era. In addition to this specialization, the area of trade has widened, until there came to be a series of markets for each

special line of distribution. Cotton, grain, machinery, clothing, and many other lines of business have developed their special markets and special organizations.

These markets may be first differentiated or classified on the basis of their relation to trade areas or territories. It is a common observation that distribution takes the form of a series of widening circles, and this gives rise to market centers of varying importance. At each market are found special traders more or less closely associated. As a result, we find certain well-recognized world markets for given lines of trade. Among the more conspicuous are Liverpool, New York, Paris, and Bremen. For certain lines of distribution these markets rule. Further, for domestic trade, we find a number of primary markets, such as Chicago, New Orleans, Minneapolis, St. Louis, and others. Of still lesser importance are the intermediate or secondary markets, serving a still narrower trade area. Finally, we have the local market.

Obviously, as we pass from the world and primary domestic markets to the local markets, the commercial organization becomes less complicated. At the larger markets are found the wholesaler, jobber, and commission firms. These are sometimes grouped into special exclusive organizations for mutual protection. But at the local markets will be found the retailer, whose

position is individual, with little or no organized co-operation.

In another place we shall show how these markets are linked together in each line of business. It must be noted that in some instances they are virtually obliterated through direct buying and selling and by trade agreements. In the discussion of the legal aspects of business we have called attention to the creation of central selling organizations which unite and make effectual the selling policy of several firms of given lines of business.

In addition to the classification of markets on the basis of the trade territory, a still further division must be noted. A study of the organization of the various markets shows that those established for the distribution of raw materials, and especially agricultural products, possess different characteristics than those established for the distribution of manufactured products. In each instance there will appear certain exceptions, but in the main the organization of the two markets are essentially different.

The essential difference lies in the fact that the distribution of raw materials, and especially that of agricultural products, is accomplished, with few exceptions, through a series of exclusive competitive markets or exchanges, while, on the other hand, the distribution of manufactured wares, with few exceptions, is carried on through

the bargaining system, or by direct selling. The dominant feature of agricultural distribution is the presence of a series of exclusive markets with strong speculative tendencies. This is particularly true of grains, cotton, live stock, produce, and tobacco. There are some slight differences in detail in each of the above lines, but the basic principles are essentially identical.

The result is the organization of exclusive markets established and controlled by a special class of traders. Naturally, those organizations are most highly perfected at the central markets. In a later discussion it will be seen that these exchanges are highly developed, and provided with rules and regulations for trading. They are organized for well-known lines of agricultural distribution.

An examination of the organization and methods of the market for the distribution of manufactured products shows that there does not exist any exclusive class of traders constituted as boards of trade or exchanges. There are well-known central markets to which the traders in a given line of business go. But the methods of the market are based upon personal inspection and bargaining. The buyers do not meet in competition at a given place and time, and transact their business according to rules laid down for all. There does not exist for machinery, clothing, drugs, boots and shoes, and innumerable

other articles, any exchange market, but rather a number of distributing points at which will be found the offices of the leading manufacturers, wholesalers, and commission men.

Thus it will be seen that the organization of the markets for the distribution of raw materials and manufactured wares have had a different evolution. The two markets in their initial stages were based upon the bargaining principle, but in more recent years the principle of auctions, or competitive bidding, confined to an exclusive class of traders, is usual for most agricultural products. On the other hand, the sale of finished wares is not restricted to any given class of buyers and sellers; but there is an open market to which all may come, and which still retains the principle of bargaining as the basis of selling. For these reasons the two markets must be considered as separate and distinct in organization and methods.

IX

EXCHANGES

In the foregoing discussion it was shown that recent changes in distribution have given rise to special associations of traders. It was further indicated that the risks of marketing certain products on a large scale necessitated mutual co-operation on the part of dealers and merchants, which led to the organization of these associations, with their special rules and regulations. They had their origin in Europe, and their dealings were confined at first to the stocks and securities of industrial companies, and the increasing volume of these securities suggested a specially organized market. As a result, at the important financial centers stock exchanges were organized. At a somewhat later period the same methods were applied to the marketing of agricultural products. This evolution led to two classes of exchanges: the Stock Exchange, where stocks and securities are bought and sold; and the Produce Exchange, where the marketing of raw materials, such as wheat, cotton, live stock, etc., and some manufactured commodities, such as dairy and packing products, could be carried on.

We are here especially concerned with the

organization of the Produce Exchange. These are of two kinds, general and special. The general exchange is one on which several commodities such as cereals, flour, eggs, dairy products, pork, etc., are dealt in. The Board of Trade of Chicago is a good illustration of the general exchange, since it admits to its list of commodities flour, grain, provision, hay, and dairy products. On the other hand a special exchange is one on which one article alone is sold, such as cotton, tobacco, petroleum, coffee, or leather. Examples of these special exchanges are the Cotton and Tobacco Exchanges of the southern markets, the Produce Exchange of New York City, the Live Stock Exchange of Chicago, and the Chamber of Commerce of Minneapolis for grain.

The essential difference between these two classes of exchanges lies in the nature of the commodity bought and sold, and not in the differences of organization or methods of business. In each exchange traders are brought together for mutual protection while trading in certain stipulated commodities. In each case the exchange is the regular meeting of merchants and commission men for the buying and selling of commodities admitted to the list.

It should also be borne in mind that all the boards of trade do not fall within the scope of our discussion. In many cities we find associations of merchants organized for promoting and

developing commercially their city and surrounding territory. In some instances these are Governmental institutions, as the Board of Trade of England, organized about 1636, and which has exerted a marked influence upon English commercial policy; it is an arm of the Government for the purpose of fostering trade and commerce. In the United States these non-trade associations exist in many cities, and are organized for the discussion of economic subjects. Our National Board of Trade meets annually to discuss the larger phases of our national commercial policy. The recent organization of the Federal Department of Commerce can be directly attributed to the efforts of this national board.

Many trading associations or exchanges can be traced back to these non-trading associations. This is true of the Chamber of Commerce of New York City, which was organized in 1768 to promote trade. It did not assume the trading functions until a later period. The Board of Trade of Baltimore was organized in 1821, Philadelphia in 1832, and the Boston Chamber of Commerce in 1836, as non-trading associations. At present there exist as many as ten chambers of commerce and twenty boards of trade in the United States which were in the beginning non-trading associations with limited charter privileges. It was, however, an easy step to convert them into trading

associations. The members were often dealers in securities, cotton, grain, and produce.

An exchange, or board of trade, is a group of traders who agree to abide by rules and regulations governing the purchase and sale of commodities, or securities. They agree to create a market, and protect it for their individual and mutual benefit. A Produce Exchange is therefore distinguished from a Stock Exchange, only in the character of the trading. The former is organized by traders in agricultural products. The most important boards of trade or Produce Exchanges in the United States are the New York Produce Exchange, New York Cotton Exchange, Chicago Board of Trade, New York Coffee Exchange, and New Orleans Cotton Exchange, Live Stock Exchange of Chicago, Chamber of Commerce of Minneapolis, Duluth Board of Trade, Merchants' Exchange of St. Louis, and Richmond Tobacco Exchange. There are many lesser exchanges with trading functions in the cotton, grain, and live stock belts.

These associations are incorporated under the laws of the State in which they are located. They are regulated directly, or indirectly by law, and in some instances very closely controlled. As a result of incorporation, they enjoy special powers and privileges, and some of them possess a quasi-judicial power, together with all necessary authority for disciplining their own mem-

bers. Among the powers granted by the State is the right to acquire limited property. The association controls its membership and frames its rules and by-laws. The most important function is the power to select, inspect, and grade the commodities bought and sold by the members of the association.

The organization is perfected in the same manner as other corporations by the election of a president, vice-president, and directors, who together constitute the Board of Directors. The management, appointment of committees, the formulating and enforcement of the rules and regulations, devolve mainly upon this board. Each member of the association has voting privileges in the election of officers and in the determination of the board policy.

Memberships in these associations are always limited in number. They are kept exclusive by the ability of a small number of members to prevent a new applicant from securing membership. The general business benefits obtained by membership in these organizations is of considerable value in dollars and cents to the merchants operating in these fields.[1] Thus buildings or warehouses owned by these organizations give intrinsic value to the membership, and the various benefits

[1]The last sale of a privilege of membership in the Chicago Board of Trade was made at $2,800. The last sale of a membership in the New York Stock Exchange was at $95,000.

combine to set a very high value on many of the more important memberships in the larger trading centers. A "seat," or membership, in the New York Produce Exchange is worth several thousands of dollars.

The Chicago Board of Trade is typical of organizations of this character. It is empowered to appoint inspectors "to examine, measure, weigh, gauge, and inspect flour, grain, provisions, liquor, or any article of produce or traffic, commonly dealt in by its members." The certificates of such inspection, as to quantity and quality, are binding upon all members. The principal exception to this sweeping grant of power is the inspection of grain, which has been made a State function, under the direction of the State Board of Warehouse and Railroad Commissioners. In addition the Board may constitute and appoint committees of reference, arbitration, and appeal, and frame rules governing their action. The final decision of the committees is binding unless an appeal is made to the circuit court within a prescribed time. These quasi-judicial functions greatly strengthen the power of the governing body over the members. The corporation is permitted to conduct any business usually carried on by boards of trade and chambers of commerce.

With the general organization before us we may now examine the regulations governing the trading. The preamble to the Board by-laws

states that the object is to maintain a commercial exchange, to promote uniformity in the methods of commerce and usages of insurance, to inculcate principles of justice and equity in trade, to adjust speedily business disputes, to disseminate commercial and economic information, and, finally, to promote the spirit of co-operation in the furtherance of the legitimate pursuits of its members. There is thus created a market with prescribed grants and limitations.

The president is responsible for the proper conduct of business, and has a limited power to suspend members for the violation of the rules and regulations. The Board of Directors, however, wield more important powers. It is, in fact, the principal repository of the powers of the association. The business and financial affairs, a large power of appointment, as well as the framing of rules and regulations are delegated to it. The directors appoint a secretary, assistant secretary, treasurer, inspectors, gaugers, weighers, measurers, and such other officers, clerks, assistants, and employees as are necessary to conduct its work. They also fix the compensation of these employees. Moreover, they may suspend the members who fail to abide by the rules in settling contracts, or expel any member guilty of any unmercantile trading. All trading orders must be executed in Exchange Hall during the hours of regular trading. Any member in regu-

lar standing who accepts orders from and acts as agent for a member who has been suspended, makes himself liable to suspension or expulsion. The directors are also empowered to fix the grades and supervise the inspection of the various commodities dealt in on exchange. They also examine the various store-rooms and warehouses with reference to safety and fitness for the storage, and issue to their owners certificates of regularity.

A statement of the powers of the governing authorities is not complete without a brief examination of the duties of the committees on arbitration and appeal. All disputes and controversies over contracts and settlements are brought before the Committee on Arbitration. Its decision is not final, but may be taken to the Committee on Appeals. This committee reviews the findings of the Committee on Arbitration, and may remand the case to the committee for a new hearing, or it may enter its own decision. The parties to the controversy usually sign an agreement to abide by the decision, otherwise they may appeal to a regular court.

The duties and responsibilities of the members of the Board are set forth in the rules. A member is held personally liable in trading until the principal whom he represents is made known. In no case can the broker designate the name of a person, firm, or corporation as the principal unless the member is in regular standing. This

rule, however, does not apply to contracts between members of the association, or between authorized representatives of transportation, insurance companies, and bankers. In all such instances the agent or broker shall be held liable for the fulfillment of the contract. Special membership cards are issued by some exchanges.

The rates of commission are likewise fixed by the rules, and vary with the character of the commodities dealt in; for instance, the rate for grain is one-eighth of a cent per bushel, while that of "D. S." (dry salted) short ribs is 12½c. per thousand pounds. In case the dealing is between members, the commission is one-half the regular rate. Another schedule of rates governs where the members buy personally, but settle their contracts through other members of the association. No member is permitted to "clear" any trade which is not for his own account. He may, however, receive orders from another party, and fill them himself. In this manner the members are protected by making it impossible for firms or corporations to secure membership rates except under special circumstances. No person can represent two firms in the same transaction.

In order to protect the regular trading, the Board fixes the place and hours of such trading in great detail. No trade or contract for future delivery can be made or offered by any member except at the place designated and during the

hours prescribed by the rules. All other trading is irregular, and should difficulty arise out of trade so made, members could not appeal to governing bodies and sub-committees of the Exchange for enforcement of their rights under the rules. "Cash grain," however, can be traded in between members at all times.

We may now turn to an examination of the kind of commodities bought and sold on the Chicago Board of Trade, and note the most important rules governing each line of business. A special set of rules, formulated by special committees of the Board, governs each class of commodity, and special expert inspectors are appointed for each class. Available warehouses are selected by proper committees and declared "regular," or satisfactory for the handling of each class of commodity. Thus with regular inspectors working under uniform standards of weight, measure, and quality or condition of commodity, and with warehouses pronounced acceptable, or "regular," a uniform working basis is established. When any portion of any commodity is received into a regular warehouse, the superintendent in charge is thus qualified and permitted to issue to the owner of the commodity a receipt duly signed and properly registered, which may from that time on pass freely from hand to hand as representing an exact quantity and quality of any given commodity.

Let us examine, first, the system of inspection. In many States the inspection is made by public officials; this is true especially of grain inspection. The State of Illinois was one of the first to establish public inspection. A State Board of Railroad and Warehouse Commissioners has supervision over this feature of the business. State inspection has followed because the farmers feel that the grain dealers are unfair. All cars loaded with grain received from country points into Chicago are reported promptly by the railroad companies to the grain inspectors, who visit these cars with mechanical devices, which obtain representative samples of the grain in the car. The grain doors are then resealed with the inspector's seal. The samples are taken to the trading floor, and turned over to the grain mechants to whom the cars have been consigned from the country. The car may then be sent to a regular warehouse and receipt obtained. This receipt is placed with the sample on the trading floor, and becomes the basis for the purchase and sale of this particular quantity of grain. As the grain changes hands by purchase the warehouse receipt is endorsed by the new owner.

The inspection of all commodities is essentially similar, having in view the securing of a sample representing fairly the bulk from which it is taken. The object in all cases is to permit the interchange of commodities by grade without the

examination of all of a specific lot when sale is made. The principle of the warehouse receipt is the same in all cases. In order to accomplish this, the commodities must be inspected, handled, packed, or stored in accordance with the rules of the Board and the State law. A commodity is delivered by the tender of a warehouse receipt. These are issued by those firms whose warehouses have been declared regular. Their stock may be sold out as cash grain by samples, but not as contract grain. Since the warehouse receipt is so important, the responsibility of the superintendent of the warehouse in preventing the commodity in his care from becoming tainted by contact or mixture with other grades is very great.

Naturally, the inspection varies with the kind of the commodity. Peculiar difficulties attend the grading of some agricultural products, such as tobacco, flour, live stock, etc. This is due to the fact that special lots of such commodities have an individual value, which would be easily impaired by mixing them with any other lot when in the warehouse. These conditions have prevented the grading of tobacco so as to establish a definite contract grade on the basis of which trades for future might be made. The samples and lots which they represent are essentially inseparable. For instance, the certificate must indicate the lot of flour, its size, whether it is

musty, hard, sour, soft, unsound, slightly unsound, etc., in quality.

In summarizing the various grades of commodities, recognized by the Chicago Board of Trade, it should be noted that they are not uniform for all markets. An attempt has been made to secure uniformity of grade for a given line of commodities for all markets, but with only partial success. For instance, the grades of wheat at Chicago are not identical with those at Minneapolis or Duluth, doubtless due to the fact that Chicago is the great winter wheat market, and the former cities are the great spring wheat markets. The tobacco grades are also local, or sectional, and correspond only in a general way with other markets. The cotton grades are more uniform, because they are fixed by one or two markets, and are based upon one grade of cotton. Although the Liverpool grades differ slightly from the American grades, yet there is a striking uniformity in both cotton markets.

The condition of climate, methods of cultivation, and handling of the commodity form the basis of grading. The object is to separate the various commodities into grades on the basis of soundness, color, and freedom from impurities. This is essentially the basis for the grading of all commodities, although other special characteristics may be sought.

One illustration will suffice to indicate the

method of grading the commodities on the Chicago Board of Trade. The classification is based upon the line of business. Accordingly, we have grain, provisions, hay, field seeds, etc. Those are further divided as shown by grain. This line falls into wheat, oats, corn, rye, barley, etc. At this point is introduced the principle of grading which is based upon soundness, color, and freedom from impurities. In some instances the principal grades are divided into sub-grades. The same principle applies to all commodities. The purpose is to discover dominant characteristics which give to the commodity varying commercial values.

Considerable controversy has arisen from time to time over the power of the Board to designate the places of storage of commodities dealt in. The independent warehouses have disputed this power, but the Board has been too strong for successful resistance. Certain rules have been laid down by the directors, governing the location, safety, and means of handling the commodities. The proprietors are required to give evidence of unquestioned financial standing. The warehouse must be easily approached by railroads and vessels, and be provided with the means of handling the commodities rapidly. They are required to assist in securing correct registration, and to extend all possible assistance

in protecting their warehouse receipt. The penalty is the withdrawal of regularity.

The warehouse committee must examine the books of the proprietor at least four times each year, but it reserves the right to make an examination at any time. They are empowered to employ experts to examine the quality and condition of the grain in order to compare it with the State grain warehouse records. The official Board of Trade weigher must weigh all grain received and sold out of the warehouse, and keep a record of outgoing and incoming receipts. All this precaution is necessary because of the great importance of protecting the warehouse receipt. The warehouse must always have on hand quality and quantity of commodity as represented by warehouse receipts shown by it.

We have thus far been dealing in the main with the external features of exchanges; we must now turn to the inner organization. We have already noted that the Board of Trade is an association of traders, leagued together for mutual protection by rules of their own making. They organize their own market, and have jurisdiction over the membership, commodities dealt in, inspection, weighing, storage, registration, grading, contracts, and finances. They have organized a market for themselves with all of its tangible and intangible features.

We must first examine the place designated

for the actual trading. This is commonly known as Exchange Hall. It is the home of the association, and is usually a large building with commodious rooms, equipped with all the aids of the business, and filled with busy clerks for the record of the sales. One portion of the main floor is set aside for sample trading, while in another part is found one or more pits for contract trading. Here is the center of information for all the known markets, and in rapid succession all possible data concerning supply and demand, and trading in other markets are recorded. In the same building are located the offices of the association and those rented to brokers and commission firms.

The Exchange Floor is the place where the buyers and sellers meet regularly for the transaction of business. The members may be either regular dealers, who are purchasing large quantities of grains, ordering it loaded into cars in Chicago and selling it on the Atlantic coast or abroad where it is consumed, or they may be dealers who are making trades on instructions from their principals whose identity is always given before the final record of the trade is made. These brokers may be trading for regular dealers, as above described, or for parties who mean simply to speculate on the rise and fall in the prices of the grain, and intend always to close their transactions before the grain which they

have bought or sold for future delivery is either delivered to them or called from them. Brokers may also represent dealers who are not members. A dealer may or may not be a member of the Board. The broker keeps all the records of transactions he makes and is responsible for their full settlement with other brokers.

The traders on the Board of Trade naturally fall into two classes, representing the supply and demand forces, and in the language of the Exchange they are called "bulls" and "bears." A "bull" is a person who anticipates that the price will rise before he is called upon to accept delivery of the grain. This gives him an opportunity to sell at a profit before that date. A "bear," on the other hand, is a trader who anticipates that the price will decline before he is called upon to deliver the grain he may have sold. This gives him an opportunity to buy at a profit before that date.

In some grain markets an insurance feature of trading is introduced, known as "privileges," or "puts and calls." A "call" is the right to purchase customarily the following day during trading hours at a specified price. It is a contract in the form of an option compelling the seller to deliver to the buyer the amount of the commodity named, if the latter so desires. A "put" is the reverse of a "call." It is the right to sell customarily the following day during regular hours,

at a specified price. It is a contract in the form of an option compelling the seller to accept from the buyer the amount of the commodity named if the buyer so desires. "Calls" are always at a price above the market price, while "puts" are at a price below the market price. A "straddle" is the buying and selling of a "put" and "call" at the same time, leaving the trader to exercise his choice. Trading in these "privileges" takes place during specified hours, both before and after the "regular" trading hours. The cost to the buyer of this form of insurance is one dollar per thousand bushels. Technically this is called "curb" trading.

There are two kinds of transactions in the Exchange market—(a) trading in the commodity for immediate delivery, and (b) trading in contracts for delivery at a specified future date. In some lines of trading the future contract is either entirely absent, or forms a minor feature of the market. This is peculiarly true of the leaf tobacco market which is a "spot" or cash market. An attempt was made to apply to this market the principle of "features," but it was unsuccessful. The value of the leaf is so individual that it cannot be bought and sold satisfactorily by grades, and the "future contract" is based upon successful uniformity in grades. This also is true of live stock, so that "contract tobacco" and "contract cattle" are unknown, except in the limited sense

that leaf tobacco may be sold on order through specific samples. Other agricultural products, however, are bought and sold on "future contracts." This is true especially of grain, cotton, and dairy products.

We shall first take up the sale of commodities on the spot market, for the reason that this is the simplest form of trading. This method of buying is followed where specific lots are desired, and where an inspection of samples is necessary. When the commodities are consigned to the dealer at the central market, they are graded and sold. The samples are brought to the office of the commission salesman, and are there displayed or taken to the floor of the Exchange, and placed in convenient boxes or pans on the tables for the inspection of the buyers. These transactions are conducted in a quiet manner, and have none of the noisy features of the pit, where future contract trading is carried on. The commodities bought and sold through samples are sought generally by manufacturers or shippers. A great deal of trading by this method occurs outside of Exchange Floor, and the commodity is often sold without grading except in a very rough way. This trading is less speculative, although every trade has a speculative side to it. But the difference lies in the fact that the "spot" market always has a specified lot under consideration, and purchases are made usually through samples.

Traders in futures are of two classes—(a) parties who buy "cash" or "spot" wheat and immediately sell a "future" so as to "hedge" their transaction and protect themselves from loss in case the price declines (if the price of both the cash and the future advance equally, there is, of course, no gain or profit); and (b) those who buy and sell purely on their judgment as to whether conditions will cause the market price of the "futures" to rise or fall, they contemplating closing their trade at an early date and reaping a profit. If their judgment is incorrect, they must pay a loss; these are purely speculators.

It now remains for us to note the main features of the purely speculative markets, or what is generally known as dealing in futures. Contracts are made, for instance, during the months of July or August to deliver a specific quantity of a commodity at any time the seller desires during the month of September, *i. e.,* "for September delivery." The quality of this commodity is thoroughly understood to be the "contract grade" as prescribed by the rules of the Exchange. Instead, however, of the purchaser having to make payment in full, it is possible by a system of differences to make only partial payments until the final delivery is made. This is shown in the following supposed case:

Suppose on March 10th A sells B 5,000 bushels of wheat for May delivery at 95c. On each day

hereafter this price fluctuates, and as the price rises above 95c., B, having the wheat, would thus be the gainer as market advances, and A the loser; so A would pass checks to B for differences in value figured on the basis of the closing market prices each day. As market prices lower, B would pass checks to A for differences shown. Let us suppose that by April 20th the price had gone up to 97½c. per bushel. Then A would have paid to B a total of 2½c. per bushel and B decides to sell to C, who finds on May 1st that price is still 97½c. A would then deliver the wheat to B in the form of warehouse receipts, which call for the actual wheat, and for these C would give A payment for the total on a basis 97½c. per bushel; but he has already paid B 2½c. per bushel, so, while the wheat costs C 97½c., A realizes but 95c. for it, B having taken the difference. B is in this case purely a speculator, having judged that conditions of supply and demand would bring about higher prices, and acted on his judgment. B may have, however, sold to D, and D to C, and C to K, and K to X, of the same wheat, between March 10th and April 20th, each of these traders having gained or lost as the market price fluctuated from day to day. These various parties, whether trading directly for themselves or through brokers, were thus speculators, though not one of them in selling knew whether or not he was selling to C, the

actual receiver of the wheat, or to a genuine speculator. When B sells to D, he closes accounts, and withdraws from the transaction except as shown by the records.

A person who desires to deal in futures, if not a member of the Exchange, must employ a commission merchant or broker. He instructs his broker as to his desires, but the broker requires of him first a deposit as a security which is known as a "margin." This deposit is on a basis of so many cents per bushel or bale. The broker or his employee then goes into the "pit" and executes the order of his client. The broker's private records show the client's deposit and a memorandum of the futures purchased or sold. The broker, however, is accountable for the trade to the clearing-house of the Exchange, on the records of which the transaction also appears until finally closed.

Another method sometimes employed for making final settlement is known as "ringing out." Let us suppose that A sells to B a given quantity of a commodity of contract grade at a price of 90c. per unit. The ownership of this is evidenced by a warehouse receipt. The future market closes that night at 91c., so A passes to B a check for one cent per unit. The next day B may sell to C, and he, through others, to K, and the market closes that night at 90½c. Checks are passed between all parties for differences

between prices at which purchases and sales are made, with K having paid ½c. to J. The process continues up to X, why buys when the market is at 95c. Differences have been passed, until X has had to pay to W, from whom he made purchase, 5c. per unit, and to A 90c. per unit. In this way the ring is made complete, each trader intervening between A and X being able to secure his profit or pay his loss promptly, and obviating the necessity for the Clearing-House.

An improved method, however, is found in the Clearing-House. In order to facilitate the settlement of contracts clearing-houses have been established in connection with the various exchanges. The institution was doubtless suggested by the clearing-houses of banking centers. A central office or establishment where each member could settle or clear his transactions is found to be highly desirable.

The Clearing-House is organized independently of the Exchange. Its function is to keep a record of sales and to open up accounts with the members. At the close of each day's business, instead of the contracting parties searching out each other, they settle with the Clearing-House and checks are passed to it to cover losses, and received from it to cover profits. "To clear" is to pass the settlement to the Clearing-House. The institution is created by the Exchange members

for their convenience in settling sales. Its officer frame their own rules and regulations.

The final settlement of closing out of thes "futures" contracts is simplified by the Clearing House and its complete records. In the abov supposed case, when C traded with B, then C's name appeared at the close of that day's busines on the Clearing-House records, and when C made an opposite trade with D, then D's name appeared on the Clearing-House records, but C's obligations were closed and his name dropped. This process continued, showing always the original trader A and the last trader up to X, who, on delivery day, was shown to be the actual purchaser of the commodity. Mr. A would then present to the Clearing-House papers evidencing his ownership of the commodity. The Clearing-House clerk would pass these promptly to Mr. X, and instruct him to make full payment to Mr. A, who thus becomes the new owner of the commodity.

With this account of the methods of making and closing future contracts, we may note in more detail their relation to the business of agricultural distribution. We have already pointed out that, wherever it is possible, agricultural products are graded, and rendered easily transferable, by issuing against them warehouse receipts while in storage. The presence of this negotiable instrument leads to the development of speculative trading among the members of the

Board, and through them among outside parties. In order to simplify such trading, the nature of these contracts is defined and provision made for their settlement. The future contract, thus based upon the actual or prospective supply, is measured by the visible or prospective demand for the commodity.

The warehouse receipt or warrant, enables the transfer of ownership without the transfer of goods; this encourages speculation. The nature of the future contract is essentially the same whether it is used in grain, cotton, or produce trading; they differ in detail only. The contract is made upon the basis of a specific grade, and deductions or additions are sometimes made for other grades. This is true especially of cotton. There is thus established by the Board a "contract grade." Any commodity dealt in by the Exchange which has been regularly inspected and shown to be of stipulated quality is considered as being of "contract grade." In this manner the contract for future delivery has reference to specific qualities designated by a commercial body, with the conditions as to quantity, quality, and time of delivery fully stereotyped, with the price to be determined by the contracting parties. These contracts are bought and sold on the floor or in the pit, and are at once recorded for the purpose of clearing.

The speculative features of agricultural dis-

tribution have been highly developed in recent years. They grew out of an attempt to forestall the future supply of the commodity. The development of the warehouse receipt and grading have made this form of trading fairly easy and accurate. The early form of warehouse receipt represented several lots, but gradually came to be applied to grade as well, thereby assuming a more elastic form for trading purposes. For instance, having first a special application, it has now become general as to quality and grade. Warehouses and elevators have also multiplied under the supervision of exchanges, holding vast quantities of contract commodities.

The future contract trading was applied to grain in the West earlier than in Eastern markets. The general contract is not used in cotton, but the contract grade is designated as the middling cotton. A great deal of popular disapproval exists against the practise of trading in futures. This form of trading is looked upon as speculative only, and that it has no wholesome bearing upon regular distribution. The greatest objection urged is that the exchange members fix the price of farm products through speculation; it is frequently called gambling. The critics, however, lose sight of the fact that future contracts are based at bottom on the commodity itself, as it arrives from the country.

The dependence of the local and secondary

markets upon the primary market is quite definite. The traders at the primary markets are experts. Their sources of information are the most accurate possible. Through the competition of these traders prices are kept uniform, and great fluctuations are avoided in normal times. This information is likewise ultimately the property of the producer, dealer and manufacturer, and even of the farmer. It extends throughout the whole trade. The farmer knows from day to day the price of his products, and also the probable supply and demand.

Under the earlier bargaining system great risks were assumed, because of the probability of great fluctuations, and without the possibility of shifting these risks to a special class of traders. The present methods of the Board of Trade contrast sharply with the continued imposition and fraud in trading where values are unknown, information is concealed, and where the absence of uniform grades compels the inspection of each piece.

Special and accurate information is gathered, and utilized by a class of expert traders. The Board trading fixes the authoritative price for each commodity dealt in. It goes instantly to every kindred market and to wayside dealers. It goes out in the market reports and through the columns of the daily press. It is common property both for producer and consumer alike. The influence of the genuine speculator upon prices

must not be overlooked. By dealing in futures he keeps the market in rapid motion, enabling the miller, manufacturer, shipper, and country elevator merchant to secure uniform prices whenever they desire to trade or hedge in any considerable quantity.

The prices which rule on the floor of the Exchange are the result of a competitive market. Bids and offers follow in frequent succession. The risks involved in moving the commodity from the farm to the point of consumption are exceedingly great. Stable prices reduce these risks, and, in addition, by hedging, they are shifted to a large number of persons. Certainty, rapidity, and economy are thus fostered. The commodity passes through a score of hands before it finally reaches its destination under the future contract system.

The final test of the utility of future contracts in the conduct of ordinary trade operations must be found in the use to which they are put by the producers, spot-cash dealers, and manufacturers. Hedging is employed by most dealers, warehouse men, and manufacturers to protect themselves against losses due to market fluctuations. It assumes in this respect the form of insurance by shifting the risks upon the speculator. A grain dealer buys 10,000 bushels of grain at the local market. He at once sells a contract for the same amount on exchange through his broker, pending

the disposal of his spot grain. When this is sold, he buys up the contract, and his original purchases are covered and his profits are fixed.

Again, a miller has an order for 10,000 barrels of flour. In order to protect himself against the price quoted, he buys a "call" for 50,000 bushels of wheat, the amount necessary to manufacture 10,000 barrels of flour, and at a fraction of a cent above the market. This insures him against loss in case he is compelled to buy his wheat. In some States trading in "puts" and "calls" is illegal. It is prohibited in Illinois, but is legal in Wisconsin. Where these cannot be used, the merchant can direct his broker to buy a future contract. He is thus insured against advance of prices, although the contract itself may be bought and sold scores of times before finally cleared. Spinners of cotton protect themselves in forward shipments of yarn by selling cotton in advance as a hedge against the stock on hand at the mill.

Hedging is universal in the grain and cotton business. It is safe to say that nine-tenths of the cotton and grain are hedged during distribution. If these commodities had to be bought by sample alone, or by personal inspection, it would increase enormously the number of agents engaged in buying and selling, and vastly complicate the whole system. More capital would be required, and expense on all sides increased, which

would ultimately come from the consumer or the producer.

The importance of the boards of trade can be scarcely overestimated in their relation to the distribution of our agricultural products. They organize a highly sensitive and responsive market, conducted by alert and expert traders. The profits are kept down at a fair margin, and are in the aggregate the result of small percentages made from large and rapid trading. Small profits on a large volume is the general rule. A monopoly of commodities is the exception. A "corner" is the gaining by any one interest of control over a sufficient portion of the total supply of any given commodity so as to dictate its price irrespective of all other influences, with all the resources of capital and information at hand. The difficulties of cornering a commodity are apparent. The tragic outcome of these attempts stands as a warning against such adventures.

No better illustration of the advantages of the market for agricultural products can be given than a contrast with the methods of buying finished products. The utter absence of any rules governing the buying and selling of most manufactured wares in an open market, where a lot is subject to the bids of many buyers, leaves a vast opportunity for deception and fluctuation of prices. This kind of buying resolves itself into dickering between the buyer and seller. For

instance, it is the testimony of experienced buyers that it is very difficult to determine the value of dry-goods, because there are no fixed standards. As a result, fraud and chicanery are often practised to deceive inexperienced buyers. Variation in the price of similar grades is said to be from ten to thirty per cent. in the same city in clothing, furniture, dry-goods, works of art, boots, shoes, etc. In short, nearly every article not subject to the close sharp bidding which accompanies the marketing of agricultural products is liable to suffer a fluctuation between value and price. The tendency is to fix staple prices without regard to competition. The seller of agricultural products has at his command far more accurate information in regard to the conditions of the market than most of the expert buyers of dry-goods and other wares, where prices are not determined under a system of uniform rules and by competition. The prices on exchange are not fixed by two persons, but by the aggregate verdict of the buyers who are present in numbers. The dealing in futures permits the sale of the commodity before it reaches the market from the hands of the country elevator merchant. It enables the producer to hold or sell it because he realizes that the advance of price is not likely to be important. It takes from the farmer and the dealer the risks of the market. It carries the trade over a larger period of the year, and thus

the great fluctuations which prevail in the distribution of most manufactured wares are avoided.

Boards of trade have been styled vast institutions for the manufacture of prices; or, figuratively, they are looked upon as the storm-centers of great agricultural areas. In a sense this is true, for there is in these exchanges an unending flood of business, and dealers, producers, and manufacturers are all factors in the trading. They may enter at any time, and make such contracts as their business requires. In this way the Exchange becomes one of the most important institutions in the whole range of commerce. It is one of the most effective as well.

By way of summary, the services of the speculative class may be briefly restated. In the first place, it tends to establish stability of price; second, it distributes the risks among a special expert commercial class; third, it relieves the producer and consumer from carrying a whole year's stock for better prices; fourth, it reduces the profits of the middleman; and, fifth, it means cash to the producer and a regular supply to the consumer.

X

DIRECT SELLING

In a preceding chapter it was shown that two methods of organizing the market prevail to-day, in many respects essentially different. It was shown that some products can be exchanged by grades, and in order to protect and extend this useful fact, and to give it commercial value, Exchanges were organized, and State and Exchange inspection established. But there are many commodities which cannot be successfully exchanged by grades. This fact has led to another system of marketing, which may be conveniently denominated as direct selling.

The characteristics of the Exchange were fully presented in the foregoing chapter. It was found that in the main agricultural products are marketed through the Exchange, with its marked speculative tendencies. There are, however, some striking exceptions to this general statement, unless we consider the auction system as a form of the Exchange. But this is true only in the sense that a group of dealers is present in both instances. Tobacco leaf is generally marketed in the South through the auction system, but still these auctions are not Exchanges within

the accepted meaning of the term. At the principal live-stock markets the auction system is also found. The marketing of manufactured products, however, is carried on by the system of direct selling. Again, there are well-known exceptions to this general statement. Dairy products are graded and largely sold through the Exchange.

The essential difference between the systems of marketing through the Exchange and direct selling lies in the fact that the former is in the hands of an organized body of traders, holding privileged rights as members of an association. This means an organization empowered by the State to make rules and regulations governing inspection, grading and trading. On the other hand, the system of direct selling is conducted through an open market to which all may come. It is unorganized in so far as it does not require certificates of membership for the right to trade at a given time and place under prescribed rules.

Certain conditions have brought about a consolidation of interests, even where distribution is carried on through the system of direct selling, but it has been brought about in a different manner than by organizing the dealers into Exchanges. Organizations quite as unique as the Exchange have arisen under the system of direct selling; among these may be cited the department store and mail-order house. Specialization has

been going on here as well as in those lines of distribution which are served by the Exchange.

The system of direct selling is concerned mainly with the marketing of manufactured wares, and therefore our starting-point is the factory. The purpose is obviously to create a system whereby the factory output can be placed in the hands of the consumer most economically and efficiently. Business conditions have forced the manufacturer to give more attention to the sale of his output in recent years. He has found it often inadvisable to leave the organization of the market wholly to the wholesaler and retailer. In the midst of growing competition and a decreasing margin of profit the manufacturer must maintain his control over the market. Otherwise his continuation in business under the competitive system is uncertain and hazardous.

Confronted with these conditions, the manufacturer has developed various plans which are designed to take over, wholly or in part, the marketing of his factory output, or at least, to exercise a positive control over prices and methods of selling. These plans assume various forms, and develop varying degrees of control over the selling organization. There are three well-marked steps in the distribution of the factory output. The manufacturer may sell directly to the wholesaler, who organizes the market; or he may deal directly with the retailer; or, finally,

he may deal directly with the consumer. It is rare that any one of these methods is used to the exclusion of all others; in fact, all three methods may be employed at the same time. The choice of methods will depend upon the kind of manufacturing and the nature of the demand. If the output can be readily sent through the mails, the wholesaler and retailer can be wholly eliminated through the mail-order business.

The consumer of to-day occupies a larger place in the scheme of distribution than formerly. It is also true that the distributor has frequently used his commanding position to the disadvantage of the manufacturer. He often forced favorable trade compacts. In order to overcome this and other difficulties, the manufacturer sought relief in two ways: he began to extend his selling organization into the wholesale and retail markets, and also to exert a control over prices and the methods of selling the output. He was forced to a struggle with the distributor for independence.

One of the first steps in this struggle for mastery was to curtail competition by consolidating the competing interests or factories under one management. The methods of consolidation through the use of the corporate idea were presented in the chapter on the Legal Aspects of Business. Naturally, where such consolidation

takes place, it affects the selling policy as well as that of other departments.

The plan of consolidation that we have in mind at present is the union of the selling departments into one central selling organization. It frequently happens that the owners of factories do not care to sell out their interests to one controlling corporation, but are willing to curtail competition by uniting on a selling policy. This may lead to the organization of one sales department to conduct all important sales, to divide the trade, and to determine other matters of common interest—a policy which is sometimes extended only to the purchasing and advertising departments; the identity of the factories is still retained. A very good illustration of this plan of selling was the International Harvester Company before 1903, which was the selling organization of the various factories in the consolidation. The larger paper mills of the Northwest were so organized until the court recently dissolved the selling organization.

In some instances the selling organization is a subsidiary corporation, owned and directed by the same stockholders who own the factories; in this case common ownership of capital is the essential feature. The result is virtually the same as in the case of the central selling organization. This method has been extensively used by the Tobacco Trust, and the Standard Oil Company. It is

employed frequently to divert public attention from the fact that the larger interests are attempting to crowd the independent distributor from the field. The real business purpose is to limit competition, to economize by reducing the selling and advertising expenses, and to divert the profits of the middleman into the treasury of the owners of the factories. Recent legislation has materially limited this form of consolidation.

It is a general practise for the manufacturer to establish branch offices at the principal distributing markets, which are supported wholly or in part by the factory. Where the distribution occurs over a large territory, it is advisable to have offices of supervision at those markets that serve the principal trade territories. The central office is usually located in New York City, with the branch offices in the leading cities. This system has many advantages, among the more important of which is the supervision of sales.

The selling organization of the factory may stop with the absorption of the wholesale business; in this case it deals with the retailer. By so doing a stronger control over the selling policy is secured. In many lines of trade this elimination of the wholesaler has been virtually accomplished. The independent wholesalers are then forced to handle the goods of smaller factories, or to enter into binding contracts with the factory

interests, with the result that the jobber loses control over the prices of the trust goods.

In recent years the selling organization of certain factories has been established in the retail markets. We do not refer to the exclusive agency or the contract system, but to the plan of establishing retail stores managed from a central office. Probably the best illustration of this policy is the United Cigar Stores Company, which is reputed to be a subsidiary selling corporation of the American Tobacco Company. This company has established several hundred retail stores in the larger cities, and the extension is going rapidly forward. The chain of stores plan of selling to the consumer is employed both by the manufacturer and wholesaler, but more especially by the large retailers. The example cited above is in point in this place only on the assumption that the distributing corporation is owned by the manufacturing company. A better illustration of the chain of stores operated by the manufacturer is the Douglas chain of shoe stores and the Lipton tea stores. Each store has its account with the central office. The goods of the Douglas factories are well advertised, and as a rule at one price, and under a trade-mark.

A familiar illustration of the control of the manufacturer over the sale of his output is found in the so-called "brewery methods." In order to have a certain and constant outlet for the brew-

ery, it is customary to seek a financial interest in the retail establishments. This interest is of all degrees, from the payment of license fees to a complete ownership of the building and equipment. The primary object, obviously, is to prevent the shops from selling any other brew except by consent. The retail shop is controlled positively by the sales department of the brewery in all matters that concern competition and salesmanship. The larger brewing firms not only cover the city in which they are located, but reach out to the leading cities of their trade territory.

Another method of direct selling is found in the system of convassers and road-men sent out by factories. We do not refer to the road-men sent out to sell to the retailer, but rather to the plan of house-to-house canvass so frequently employed by book publishers and insurance companies. By this plan the articles or contracts are sold singly and not in quantities to the consumer. Territories are blocked off, and the selling organization is brought down to the consumer.

Probably the most common method of reaching the consumer directly from the factory is through the mail-order system. Especially is this method widely used in the sale of dry-goods, clothing, and novelties. The rapid growth of the mail-order business in recent years is one of the unique phases of direct selling, and, in fact, of all modern distribution. The mail-order system is also em-

ployed by the wholesaler, and even by the retailer.

These are the most common methods of direct selling employed by the manufacturer. In some instances the manufacturer does not desire to organize his sales department in the wholesale and retail markets, but does, however, deem it necessary to control the price of his output, and in other ways to regulate its sale. The system of retail stores is often too expensive, and he recognizes the danger of depending exclusively upon the distributor, and resorts to many devices to hold the interest of the consumer. He recognizes the value of cultivating directly the consumer's market.

One of the most common methods of accomplishing this is through the exclusive and limited agency system. The agency is a modified form of the retail store, operated directly by the sales department of the factory, or by a central selling organization. Accordingly, a dealer is selected by the manufacturer to handle his goods under contract. This system is extensively used. After a manufacturer has acquired a reputation for the quality of his output, amply protected by his trade-mark, and liberal advertising, he is in a position to accept the exclusive agency system. The agent is usually selected from among the retailers whose business would enable them to handle the commodity to advantage. A certain territory is assigned to the agent, and he is usually

protected in the trade of that territory. Usually all of the agent's profits go to the regular agents, even though the consumer buys directly from the factory.

The exclusive agency system is largely used by the manufacturer of high-grade products along certain lines, such as sewing-machines, hats, shoes, ready-made clothing, typewriters, automobiles, vehicles, and farm implements. The Singer Sewing-Machine Company has about three thousand agencies in the United States and Canada.

The principal features of the exclusive agency system are the elimination of competition by setting apart a territory to be covered by an agent, the determination of prices by the manufacturer, the fixing of definite profits for the agent, and co-operation in advertising. The agent is usually held responsible for collections. His compensation is either through commissions or by salary; a combination of these is also used. In this way extra effort is invited to push the sales, but the commission plan is more frequently used. The agency system permits the manufacturer to retain his control over the sale of his output without assuming the expense of maintaining an independent local establishment. It is often unprofitable for the manufacturer to establish retail stores for the sale of his goods alone; for, naturally, a certain volume of business is needed to

meet expenses and provide profits. For this reason the agency system is so generally employed by the manufacturers of high-grade goods. Among these may be named the Hannan shoe, Dunlap hat, the National Cash Register Company, Wernicke book-cases, etc. He makes use of the experience of the retailer already established in business.

Various modifications of the agency plan are devised from time to time by the manufacturer and jobber. A plan has been recently developed for the sale of cigars by the National Cigar Stands Company, a New Jersey corporation. The aim of this company is to become the sole jobbing-house for druggists, who are the agents handling the goods of this firm. It is not an exclusive agency, but is based upon a percentage of business. It will supply any foreign or domestic brand of cigars upon a certain basis of profit to the druggist, provided preference is given to their brands. The aim is to do the buying for druggists, and to furnish them with expert advice in handling cigars; at present nearly 2,000 stands are in operation.

We now come to a consideration of the methods devised to control prices and the manner of sale where there is no attempt to limit competition, nor to select any one dealer for a given territory. In fact, any wholesaler or retailer may sell the goods. This plan is generally designated as the

contract system. It is capable of considerable variation; it seeks mainly to control prices, and to that end extends rewards and imposes penalties. In a decision involving the American Tobacco Company, which refused to sell to a jobber who refused to handle its goods alone, the court held that it was not a monopoly, but was a trade agreement which could be properly made.

Three parties usually enter into the agreement. Consequently it is known as the tri-part contract plan, and is especially used in the drug business. The proprietors, jobbers, and retailers have strong organizations to protect their respective interests, and in this way they can be bound together by stipulated agreements. This contract is signed by the manufacturer, jobber, and retailer. By the provisions of these agreements, the purchase of a stipulated quantity of goods secures a wholesale price, which in turn insures the jobber and retailer a certain profit upon the sales. This plan was developed to prevent the aggressive cutter from reducing the price fixed by the proprietor to all the trade. The agreement calls for the sale of the article according to a stipulated price, and in order to prevent cutting, checks are instituted. One negative check upon price-cutting is known as the serial-number plan. When the manufacturer sells his goods to a jobber, each article is numbered, and the series sent to the jobber; this number follows the article to the consumer.

In case the retailer cuts the price, the other trade interests complain, and the article is traced back by this number to the jobber by the proprietor. The jobber is then warned that if he sells the goods to such aggressive cutters, no more goods will be sold to him. The retail interests are so organized that, although a retailer may not belong to the organization, he must abide by its rules and regulations; for, if he persists in cutting, his name will be stricken from the list of those retailers who can buy the article in question.

Another feature is known as the rebate plan, and is also known in the drug business as the Kramer plan; it is a subordinate feature of the tri-part contract. When the jobber sells to the retailer a slip is signed by the latter, which shows the amount of the purchase, and contains an agreement to maintain fixed prices. The profit of the retailer is a fair per cent. in the first instance, but when the articles are all sold, the retailer gives notice to the proprietor of the fact, and shows that prices have been maintained; the proprietor then remits the rebate of a given per cent. This operates to induce the retailer, not only to push the goods, but also to maintain regular prices. In most instances the proprietor develops the advertising campaign.

The contract plan was formerly widely used in the marketing of trust goods. It is an ordinary sale, but one with conditions attached; the rebate

was a favorite feature. It is not designed alone to control prices, but to encourage the wholesaler and retailer to push the particular goods covered by the contract. In this way the distributor was virtually the agent of the manufacturer. Rebates were given in addition to regular trade discounts in case purchases were made in wholesale quantities.

In some States the rebate plan has been declared illegal by the courts. As a result the distributors in some of the States have adopted a plan of their own. In charge of the State is an executive committee and a president, and the State is divided into sections with a superintendent in charge of each. In case a wholesaler undersells, he is reported to a State committee, and if the cut is bona fide, other wholesalers are permitted to meet it. This plan was used especially in the sale of sugar. Another form of the rebate plan is to ship free goods in addition to the amount contained in the invoice.

Because of adverse legislation, supported by the courts, the rebate plan has been largely given up, especially in the West. The same results are attained, however, through "free goods'" and by billing goods at higher prices.

Coupons and premium inducements are also employed, and even local discriminations are used to introduce goods. Probably the Florodora Tag Company affords the best illustration of the extent

to which the premium system can be used to encourage trade. It has a string of stores exchanging merchandise for tags, coupons, bonds, certificates, etc., and the business has assumed large proportions, amounting in 1902 to fully $4,000,000.

Another method of control which is widely used by the manufacturer is the package system. The practise of putting certain commodities into convenient packages at the factory has many features of mutual advantage to the manufacturer, wholesaler, retailer, and consumer. It makes possible a more economic handling of the commodities by all interests. Its primary purpose, however, is to protect the manufacturer by selling his wares under his own trade-mark; in so doing it also protects the consumer. He secures a uniform quality and quantity. The package likewise has great advertising value, for in this way the goods of a manufacturer are readily identified, not only by the package, but also by the trade-mark. It eliminates the possibility of fraud, except in the case of underweight. It saves the retailer a great deal of clerical work, and simplifies bookkeeping, because the packages are of uniform weight and price. The package system is found especially in the grocery business, and the shelves of the grocer afford striking evidence of its general use.

The manufacturer has also found that the

trade-mark and advertising have proven valuable aids in maintaining his control over the marketing of his products. The trade-mark established his position in the market for quality and fair dealing. Through advertising he makes a constant appeal to the consumer. Through these aids his relationship with the consumer becomes intimate. He creates a demand for his goods in the consumer's market, which enables him to stipulate the conditions of sale. Advertising and the trade-mark have assumed such importance in modern business that they are reserved for special treatment.

With these more important facts of direct selling before us, in so far as they relate to the manufacturer, we may now detail some of the advantages of the system. The manufacturer's interest in the market is the outgrowth of competition and the desire not only to limit this, but also to secure a more independent position in the trade. It was found hazardous in many cases to rely wholly upon the distributor; business independence was therefore sought. This could be secured by extending the sales organization into the wholesale and retail markets, or by developing a control over prices and the manner of selling.

The key to this newer trend in business is the growing appreciation of the importance of the consumer by the manufacturer; it is a struggle to control the consumer's market. The manufac-

turer is interested in a constant demand. He must know the needs of the public in order to determine the factory policy, and is especially important to the manufacturers of many lines of goods.

In addition, there are doubtless great economies in the system of direct selling from the manufacturer's standpoint. Where several factories can utilize one selling organization, a great saving in the expense of administration follows, in addition to the elimination of disastrous competition. Prices are controlled and the distributor's profit saved. Naturally, the consumer's interests are not always respected under a system of direct selling, but we are presenting the subject from the point of view of the trade.

The principles of direct selling and control of sales may be utilized by the wholesaler as well as the manufacturer, but the problem of wholesaling and retailing are special, and will be reserved for fuller treatment. While the manufacturer has resorted to the methods described above to extend his influence in the distributor's market, still, it must not be too strongly inferred that the old channels of distribution have been abandoned; in fact, it must not be inferred that direct selling is the predominant feature of the present-day market. It is, however, more largely used to-day than formerly by the manufacturer and wholesaler, and is capable of great extension.

At this point it is desirable to illustrate the principles of direct selling by a more specific reference to some of the more important lines of distribution. The anthracite coal business affords an excellent instance of the trend toward direct selling and control of prices, although apparently it is in the hands of the regular distributors. The marketing of coal in theory at least, and often in practise, is entirely distinct from mining. The commercial phase of the business theoretically begins when the mine operator delivers the coal to the selling organization, but coal is distributed either by the sales department of the mining companies, or by selling companies organized for that purpose. The organization of the bituminous coal business differs in some respects from that of the anthracite business. The main differences arise from the fact that the anthracite fields are controlled by a very few railways, although the marketing is conducted generally by separate selling companies. The bituminous fields, on the other hand, are so extensive and widely distributed that a monopoly is not desirable, or even possible at present. In the bituminous business the mine output is sold almost exclusively to the jobber, and he in turn sells to the retailer, although in the larger cities the wholesaler may conduct a retail business in connection with his regular wholesale business. Some of the retail firms buy directly from the mine, and,

again, in some cases the larger bituminous mine companies operate their own wholesale and retail yards in the larger markets. But these are exceptional, and the general rule is to sell to the wholesaler on time contracts for the delivery of specified quantities.

In order to appreciate the organization of the local business, and particularly the anthracite business, it will be necessary to note some of the conditions determining the demand for coal. The characteristic feature of the demand lies in the fact that it is not constant. The demand is for commercial and domestic purposes; for domestic purposes it is much stronger during the winter. On account of the inability to mine and transport the coal to meet this increased demand, an interesting development in the distributive organization has taken place.

Because of this seasonal demand, provision must be made to place large quantities of coal near the markets. The selling companies have their means of controlling prices and distribution in the anthracite business, and can develop any system which will permit continuous operations at the mine, as well as the maintenance of a supply for instant delivery.

The first step in meeting this situation and in bringing stability and order to the business is the establishment of large distributing, or controlling depots at available points. At these points the

coal is concentrated during the summer, ready for delivery during the fall and winter. These depots are located at the lake and sea ports, and near the larger cities, and from these points the interior and export shipments are made, and substantial encouragement in the way of discounts is frequently given to induce early purchases in order to reduce rush orders during the winter months. The function of these controlling depots, which are, in fact, warehouses, is to receive the coal from the mine, and to hold it awaiting the demand of the wholesale and retail dealers.

Some of these storage yards are of immense size. Probably the most extensive one is that of the Lehigh Valley Railway at Plainfield, New Jersey. The output of the mine of this road is dumped into these yards when not shipped directly to the dealer. They cover about fifty acres, and lie within easy reach of the various shipping lines. With these public or company yards are also linked a large number of private yards belonging to wholesalers and retailers, which provide further storage facilities.

The foregoing details have been presented because of their direct bearing upon the coal business, for they influence intimately the distribution and delivery of coal, and give stability to the business. We may now turn to the organization of the market. Coal is sold through the system of direct sales. Since climate, population,

industry, development, and transportation create the demand for coal, it is obvious that the trade will be concentrated in the North, where populous cities are located, and where manufacturing is extensively carried on. There are three coal markets: the export, wholesale, and retail markets; our interest is primarily in the domestic trade.

Coal is sold generally through the wholesaler and retailers, although the anthracite business is largely controlled by selling companies in close connection with the railways penetrating the coal fields. These selling organizations are legally wholesalers, but they may select independent yard owners to act as local agents. The primary object is to control shipments and prices. Where this method is employed, the territory is divided and prices fixed and cutting prohibited. In most instances sales are made on commission, and the commission man is virtually the agent in such cases. In other instances the jobber is employed. He has his yard at some large distributing point, and contracts for the output of a mine or a given portion, and undertakes to interest the customer.

The mine owner or operator must decide through which system, or combinations of systems, he will market his coal. Monopolistic conditions will likely determine his choice, as is shown in the methods employed in the anthracite, as compared with the bituminous, coal business. The

anthracite wholesale dealer does not have the freedom of choice that is accorded to the bituminous dealer. In the latter instance the wide distribution of coal, and the large number of independent mining interests have so far fostered competition that contracts can be placed more freely.

Probably the strongest method of control from the operator's point of view is the extension of the system of direct sales. This enables the operating companies to make a closer study of their territory through their own agents, and thereby gain a stronger hold upon the market. They avoid the placing of the sales organization in the hands of persons whose interests are not always identical with their own.

We now come to the local retail coal business. In every city, town and village we find the coal business established in some form. It is usually carried on in connection with other fuel supplies, and sometimes in connection with the lumber business, or even the grain business. Especially is this true where the demand of the local market is not sufficient to warrant an independent business.

The organization of the local coal business when conducted alone is comparatively simple. It assumes four activities: the purchasing (usually with the proprietor in charge), the selling, the delivery, and the collections.

The retail coal merchants have a strong organization to regulate their dealings with each other, but particularly with the wholesaler; in most instances a dealer cannot buy coal unless he is regular. This organization is so powerful that it has forced the respect of the jobber, and consequently the bulk of the coal sold in the local market passes through the hands of the regular dealer. At every point we find powerful organizations to adjust the apparently conflicting interests, so that harmony, economy, and efficiency are secured. This is particularly the case with the anthracite coal business.

We may further illustrate the general principles of direct selling by referring to the organization and methods of the butcher business. The larger packing-houses are invariably located near the great live-stock markets. In order to keep the factory running, it must have a constant supply of killing stuff on hand. These great packing-houses have been evolved by commercial necessity, and have displaced the smaller slaughter-houses. They have utilized materials that were formerly waste products, and refrigeration has transformed and extended the scope of the sales department. Possibly nowhere else can live stock be shipped and converted into salable products, and distributed so economically as at Chicago. We find here the largest and best-equipped packing-houses and scores of factories

that use such by-products as hides, horns, hair, blood, bones, glue, oil, grease, etc. The city itself is a large consumer of fresh and packed meats, and near it are many secondary markets. We have noted in another chapter the tendency of the packing-house to move westward nearer to the grazing and corn belts. Refrigeration has made possible the shipping of dressed meats considerable distances from the place of slaughter; obviously, the packed product can be easily shipped in any case.

We shall take up especially the distribution of dressed meats. It is well known that some fresh meats can be more easily preserved for shipping purposes. It is also well known that a larger portion of the carcass of some animals goes into dressed meats than in the case of others. For instance, the carcass of the sheep is almost invariably sold as dressed meat, and must be consumed in a comparatively short period after killing. On the other hand, beef is either canned, or sold as fresh meat.

The retail meat business has undergone several changes. It was formerly customary for the retail butcher to do his own killing. The fresh meat could not be shipped any distance because of the danger of spoiling. But with the construction of the refrigerator car the large slaughter-house can now place a constant supply of fresh meat in the hands of the retail butcher. In this

way the packing-house has extended its system of direct selling by establishing close relations with the retail butcher, or by placing its own branch store in the local market; as a result, the retail butcher is now taking more fresh meat from the large slaughter-houses. The average distance over which cattle and sheep are shipped is greater than that of hogs, a fact which has an influence upon the slaughtering and distributing business.

In several instances the retail meat dealer's protective associations have been organized to compete with the great slaughtering-houses, and to insure themselves a supply without having to meet the prices of these large concerns. For instance, in New York City, an association is building its own slaughtering establishments. Likewise in California co-operative meat companies have been organized to do a general retail business as well as slaughtering and wholesaling; its scope of operation is quite wide. Patents do not make the packing business a monopoly. It is open to all, but it is the large capital, large output, and effective organization which makes the modern packing-house a success. Recent investigations of packing business, however, indicate that rebates and private cars have vastly promoted the growth of these industries.

In the distribution of dressed meats two systems are employed: one is to sell through the

wholesaler and retailer, and the second one is to sell directly through establishments owned and operated by the companies as agents. It is customary to organize subsidiary distributing or selling companies to take the slaughter-house output, and distribute it as a whole or in part. The larger firms have their own distributing depots scattered over the United States, and even over Europe. The tendency of the packers to sell dressed meats directly through their own agencies is felt in the retail markets of many of the larger cities. This same influence has likewise reduced trading on the speculative market. The packers can eliminate speculation in two ways: first, by becoming speculators themselves in order to control prices; and, second, by selling their products directly without the assistance of the middleman. This latter policy is employed generally in the sale of dressed meats. Of course, a portion of the packing-house goods goes finally to the Board of Trade. Higher prices are often quoted to the wholesaler and retailer in order to prevent this speculative phase of the business and to build up the system of direct selling.

An illustration of the growth of the practise of direct selling of dressed meat is given by the following statistics: The branch houses of Nelson and Morris are distributed as follows: in New York, 13; New Jersey, 6; Pennsylvania, 17; Maryland, 1; Washington, D. C., 1;

Connecticut, 5; Massachusetts, 6; New Hampshire, 1; Maine, 1; Ohio, 5; Michigan, 6; Indiana, 2; Illinois, 3; Minnesota, 3; Wisconsin, 1; Virginia, 3; Georgia, 3; Alabama, 1; Louisiana, 1; Arkansas, 6; Tennessee, 1; and Missouri, 1. Swift and Company controls 36 branch houses, operating from its Kansas City plant, and located mainly in the South and Southwest. The South Omaha plant operates 15 branch houses in the Middle West and Western States; from St. Paul three are operated, and ten from East St. Louis; from Chicago the same company operates 117 branch houses principally in the Eastern cities, along the Atlantic seaboard as far south as Virginia and North Carolina; they have six branches in Boston.

The Armour Packing Company controls 53 branch houses throughout the Southern and Western States. It has 16 controlled from South Omaha, and 210 from Chicago distributed over the Eastern and Northern Mississippi Valley and Atlantic seaboard. Of this number we find 8 in New York, 4 in Philadelphia, 12 in Chicago, 5 in Boston, and 6 in Brooklyn. In connection with these branch houses butter and eggs, and poultry are extensively handled. Thirteen branch houses are operated from Kansas City for this purpose, 15 from Omaha, 13 from East St. Louis, and 49 from Chicago. The company also has 34 retail establishments to which they assign ship-

ments. These companies are wholesalers in North Atlantic States.

The National Packing Company controls a number of subsidiary companies acting in the capacity of agents, and has on its list a large number of branch establishments. For instance, the Anglo-American Provision Company controls 17 in the Northeastern States. The Fowler Packing Company, acting as commission agents, controls 18 establishments in cities; the St. Louis Dressed Beef Provision Company 16; the Omaha Packing Company, 29; the United Dressed Beef Company, 1; the Hammond Packing Company, 29; Ruddy Brothers, 6; and the C. N. Hammond Company, 77.

While this list is not complete, it fully illustrates the tendency of the packing-houses to sell their dressed meats to the consumer through branch houses as well as to sell to the retailer. This movement is comparatively recent and has rapidly grown. It has curtailed the local slaughter business in the smaller cities, and has made the local retail butcher a part of the sales organization of the larger packing-houses.

The refrigerator car has not only made possible the establishment of fresh meat branch houses at great distances from the slaughter-houses, but it has also brought within their reach the small towns through the "route-car" system. These refrigerator cars make the small towns regularly

and enable the local meat-dealer to keep his shop supplied with fresh meat direct from the large slaughter-houses.

The sale of tobacco products affords another illustration of the principle of direct selling. The manufacture and distribution of tobacco products are based upon a threefold classification, viz., smoking, chewing, and snuff. The division is carried still further in the case of chewing and smoking tobacco. For the purposes of illustrating the methods of the sale of tobacco products, we shall take cigars, for the reason that they are more widely consumed. They are sold commonly in tobacco stores, groceries, drug stores, hotels, barber shops, and saloons. This is not equally true of other tobacco brands. The retailing of pipe and chewing tobacco is confined almost exclusively to regular retail tobacco and grocery stores.

The distribution of cigars follows the usual channels employed in direct selling; most of the output is jobbed. The smaller factories frequently sell to the retailer through the jobber, but more recently some distributing houses have started a mail-order business, and in some instances, where distribution takes place on a large scale, the consumer is reached through a chain of retail stores. The principle of quantity-buying is largely used in the tobacco trade. The manufacturer establishes a jobber's list, and if the

retailer can buy in wholesale quantities, he can secure his stock as cheaply as the jobber. This tends to eliminate the jobber unless he protects himself by establishing his own retail stands, as in the case of the United Cigar Stores Company and the National Cigar Stands Company.

Where the manufacture of cigars is done on a large scale, the advantage of selling directly, either through the sales department, or by means of selling companies controlled by the same capital, becomes apparent. A better selection of leaf can be secured for the different brands by combining direct buying with direct selling. The successful distribution of tobacco depends intimately upon the successful distribution of the leaf. This relationship is possibly more intimate in the case of tobacco than in any other business.

By way of illustration, the American Cigar Company may be taken as a type of organization. In New York City it has its central office, which is divided into departments suggested by the nature of the trade, as well as the regular departments found generally in commercial organizations. The American Cigar Company grew out of the combination of various small concerns manufacturing smoking tobacco, and is reputed to be interested in the business of distribution. Its chief advantage lies in its enormous capital, and perfected organization. From its central office in New York it controls numerous branch

offices in all the principal cities of the United States.

The most important departments found at the central office are supply, manufacturing, machine, sales, export, freight, retail sales, advertising, auditing, leaf, and wholesale. The American Cigar Company is but one of the organizations presumably controlled by the American Tobacco Company, engaged in buying, manufacturing, and selling tobacco. The American Cigar Company sells cigars, another company sells plug, another sells snuff, and still another sells smoking tobacco. The territory covered by the American Cigar Company includes the United States, Cuba, Porto Rico, and part of South and Central America. For the purchase of leaf this territory is divided into districts with a superintendent in charge of each. The supply is distributed to the various factories under its control. The factories have their own assorting and packing departments. The tobacco is packed according to the size, quality, and color, which is a very important feature of the cigar business. Cigars are packed in 5,000 lots, which are called assortments. They are then placed in a store-room to age, or to become "box ripe" before shipment. The better grades are packed in large chests lined with zinc to protect their quality. In the preparation of cigars there are two prime considerations for the manufacturer. In the first place, he must see

that his cigars are made uniform, and, second, he must protect his brands.

The sales department of the American Cigar Company is obviously one of its most important ones. The sales are made to the jobber and retailer, and, through their own chain of retail stores, to the consumer. The territory is divided into sales districts, with the leading cities as centers, with a superintendent in charge of each district; this system is also extended to foreign countries. In some cities and States subsidiary companies are organized, and given a territory, selling under a price agreement. This is virtually the agency system.

The American Cigar Company is reputed to be interested in selling directly to the consumer. As a selling company, the United Cigar Stores Company has opened up a large number of retail stores in the leading cities throughout the country. These stores are similar in appearance, repeating throughout the same principles of decoration and stocking. The company has about 125 retail stores in the Greater New York territory. They are gradually buying out retail stores, or entering into competition with those which refuse to sell. The company is rapidly extending its system to the leading cities, and to-day controls several hundred retail stores, which are managed from the New York office. In addition to direct selling through their own

retail stores, the company also sells to the independent retailer and wholesaler.

In addition to the American Cigar Company, a considerable portion of tobacco is sold through the independent manufacturing and distributing houses. The independent manufacturers sell as a rule to the jobber, and to some extent to the retailer. Although the sales of the American Cigar Company are quite large, yet a great bulk of tobacco is marketed by the independent manufacturers. Some of the larger jobbers buy the entire factory output, and then place it upon the market through their own brands. We have, then, the manufacturer's brands and the jobber's brand. In some instances the smaller factories do their own selling and distributing, while others combine the jobbing and direct-selling systems.

On account of the growth of the United Cigar Stores Company, the independent retail stores have found it difficult to compete with it in the large retail markets, and in order to maintain their position co-operation has become necessary. Several companies have been organized recently in New York City, establishing a chain of stores. This is the plan employed by the United Cigar Stores Company. The object is to place under one organization a large number of retail stores so that their stock can be bought cheaply, and the whole business made uniform and less competitive. The smaller chain of stores comprises the

Waldorf-Astoria Cigar Company, A. Schulte & Company, and Robert E. Lane. These grew out of the local competition caused by the large volume of sales and uniform business methods of the United Cigar Stores Company. In competition with the United Cigar Stores Company a New Jersey corporation has been recently organized as a jobbing-house under the name of the National Cigar Stands Company. As previously pointed out, the object of this company is to do the buying for drug stores, and generally look after the methods of handling the cigar business of these stores.

Probably no better example of the tendencies of present-day distribution is found than the methods of marketing farm machinery of all kinds. Originally it was the general practise to sell the bulk of the factory output through the jobber. But the growth of large factories through expansion or consolidation has materially modified this earlier plan, and particularly the sale of certain kinds of farm machinery. The smaller factories still use the jobber, but the larger ones have eliminated him in most instances.

In the first place, farm machinery for the purpose of distribution is divided by the trade into two classes, small and heavy machinery, or, in other words, into inexpensive and expensive machinery. The first class includes wagons, harrows, drills, rakes, plows, etc., which are in such

demand that the dealer can afford to carry a large stock. These are net goods and are usually sold outright to the dealer; they are bought generally from the factory, but in some cases may be secured from the jobber. The second class includes the heavier and more expensive machinery, such as threshers, harvesters, mowers, shredders, etc., which the retailer cannot usually afford to carry in stock on his own capital. These are known in the trade as consigned or commission goods, and are almost invariably bought of the manufacturer.

The International Harvester Company affords an excellent illustration of the distribution of farm machinery on a large scale. Side by side with the efforts to excel in the manufacture of superior machinery has gone on the effort to perfect the selling policy, and the result is the creation of a most effective and highly developed selling organization. While efforts are constantly made to improve the machine, still, the perfection of the sales organization has commanded great attention recently. Before the International Harvester Company was organized the large companies were engaged in a competitive and expensive struggle for the market. A great many expenses were duplicated, and consequently losses resulted. The companies supported separate office organizations in every particular. In 1902 the six leading harvester companies established at Chicago a central office

for handling all matters of common concern. At first the office organization of the several factories was retained, and the Chicago office attended mainly to the selling, advertising, and finances. A classification of goods was made so as to minimize competition among the different factories. The sales organization was divided into five divisions, corresponding to the component firms; for instance, there was the McCormick division, the Deering division, etc.

This arrangement did not continue long, but was superseded in 1903 by the present organization. The principal result of this change was the transfer of the entire office organizations of the different factories to Chicago, leaving merely the factory organization in charge of the respective factories. This consolidation is not a combination or trust, but is the result of the complete purchase of all the properties of the different plants. The object was doubtless to bring the commercial business of all the plants under one uniform plan. The products of the various plants were competitive, and the aim was to minimize this competition and to save in various ways large expenses, such as advertising, and in the reduction of the office force. A primary purpose was to establish uniform prices to all the trade. Prices are made in the same manner as in other lines of trade; quantity buying determines the price. The company deals directly with the

retailer and never with the consumer. This policy is pursued for the purpose of encouraging the retailer to develop his local business.

With the central office established at Chicago, the next step in the determination of the selling policy was to decide whether the jobber was to be employed, or the branch-office system, dealing directly with the retailer. The goods handled by the International Harvester Company are in the main commission goods, and for this reason the branch-office system is more economic and effective. This implies the division of the trade territory into districts, which includes all countries using the output of the several factories. In charge of each district is a general agent. The district office is treated as if it were a separate business dealing with the main office. It is charged with all goods and supplies consigned to it, and with all items of expense connected with the district, and is also credited with all the sales.

The next step is to divide the district into blocks in charge of block-men. This brings the sales organization down nearer the retailer. Naturally, these blocks vary in number and size according to the extent of the district and the systems of transportation. These block-men do not receive stock on consignment, but work upon a salary. They are directed in their work by the district agent. Working under the district agent

and block-men are road-men who act as salesmen and also set up machines.

Since the greater portion of the stock of the local dealer is carried as commission goods, an annual adjustment of accounts must be made. On "settlement day" the company is represented by the block-men. The contracts usually contain "carrying clauses" which enable the retailer to carry the unsold stock over into the next year's trade. Net goods are bought outright by him. An interesting feature of the business of this company grows out of the manner of its creation through the consolidation of the several factories. For business reasons the output of the different factories is sold under the old firm names. This plan is retained for the reason that some farmers and communities want Deering harvesters and others desire McCormick harvesters, and in this way the trade value of the reputations of the old firms is utilized. In order to carry out this idea effectually, it frequently becomes necessary to select several retailers to handle the different kinds of machines of the company in the same market.

By reason of this and similar organizations the jobber's activity has been materially curtailed in the farm-implement business. The tendency of the trade is to rely upon the local dealer. At some of the larger distributing points jobbing-houses are found, but these are frequently agents

of some manufacturing firm for the main lines, and are permitted to carry side lines of jobbing stock which are not competitive.

The organization of the market for raw cotton is similar to the grain market. We desire now to point out briefly the methods of distributing cotton goods. Before the cotton has reached its final stages of manufacture, it may pass through the hands of several independent business organizations. The first step in manufacture is that of spinning and weaving, which converts the raw cotton into cloth. The different weaves are based upon the simple texture, which is produced by arranging the threads at right angles to each other. The number of threads to the square inch determines the grade of the cloth. As the shafts are increased in number, the product becomes richer and more varied.

The complex weaves are produced by varying this basic or simple texture. It is the foundation of all other types. The most important commercial forms of the simple weaves are calico, muslin, handkerchiefs, etc. Twill is the first departure from the plain weaves, and produces light fancy goods, and is known commercially as cashmere, serge, and blanket. The spinning and weaving business may be carried on side by side, but are often conducted independently; in the United States and Canada they are more often combined.

The raw cotton passes usually through some fifteen processes before the thread is finally ready for weaving. When the cloth leaves the loom in the form of rolls, it is known in the trade as a "bolt," and varies from 10 to 70 yards, according to the requirements of the trade. In the cloth rooms these rolls are finished, and assorted for the market. Frequently the conversion of the rough weaves leads to a separate enterprise, known in the trade as the converter's business. After the cloth is converted and assorted it is bolted to suit the purchaser, but sometimes it is bolted before it goes to the converter. Style and use, as well as weight, length and uniformity are important in bolting. These qualities are obtained by a careful mixing of the threads with reference to the quality and the color of the staple.

Nearly all of the cotton-mill output is sold through a commission house located at some great market, as New York City. This house takes orders for cloth or yarn and transmits them to the mill. It looks after the sale, delivery, and collections, and guarantees the account. Most goods are sold on sixty days' credit. The principal cotton-yarn market of the United States is Philadelphia, and, for cloth, New York City. These cotton mills have branch houses in Chicago, St. Louis, and Cincinnati. The manufacturer may also sell to the jobber without the aid of the commission firm. It frequently happens that the

converter buys his own gray goods, and converts them into grades, while another house puts on the finish through bleaching, folding, and coloring.

The commission-houses handle cotton cloth almost exclusively. The yarns going North are sold to weavers, who do their own spinning. Many of these weavers use a great variety of yarns which would not warrant them in spinning; some, for instance, use cotton warps and wool fillings. The mill products may be consigned to the commission man, and drafts of 75 to 90 per cent. of the value of the goods drawn against them.

Some mills have an office in New York City, and sell directly to the jobber, while some employ salaried men to sell to jobbers in certain territories. Most of the mills of the South sell through commission-houses. It frequently happens that this relationship is quite secret, the first often advancing money to the mills. It thus appears that a commission firm not only sells the goods, but also assists in financing the business.

In England the cotton-mill products are sold on commercial exchanges. In Manchester there is a large Exchange building, where the manufacturers and brokers meet daily. Attempts have been made to introduce this system in Philadelphia. This approaches the methods of the Exchange, and would doubtless lead to the

development of better standards of grading, as well as to more uniform values.

The above facts relate to the marketing of cotton goods. Woolen products are sold on a somewhat different plan. The output of the woolen mills goes mainly into clothing and blankets. It was formerly the custom to job these goods to the retailer, but the more recent tendency is to eliminate the jobber and deal directly with the mills. The output of the woolen cloth mills is sold to two interests: first to the manufacturer of ready-made clothing, and, second, to the tailor merchant. The latter secures his piece goods of the agents of the mills, especially if his trade is large; if not, it is more frequently bought of a jobber. The tailor merchant sells the cloth to the consumer, and converts it into wearing apparel.

The demand for ready-made clothing has increased enormously during the last few years. As a result, several large houses are engaged in making trade-mark goods of a high quality. In addition, the city department stores draw large stocks manufactured under their own trade-mark. This has transformed the ready-made clothing business, since these manufacturers buy their cloth directly from the mill. It is in the marketing of their output that the newer trend is more apparent. Formerly ready-made clothing was of a cheaper grade, and was sold mainly through

the jobber. But the demand for high-grade clothing has built up the trade-mark, which has brought about a different method of marketing. The favorite plan is to select some reliable retail merchant and give him the agency for his city or locality. In this way the jobber is virtually eliminated in the sale of ready-made clothing, and especially in the high-grade trade. The manufacturer deals directly with the retailer, who has exclusive rights for his territory. In the larger cities the manufacturer also frequently has a chain of several stores to sell his output. In the ready-made clothing trade the jobber is fast losing ground, and in his place has come the agency store, and, in a limited way, the chain of stores for the city trade.

The big retail stores buy from seventy-five to eighty-five per cent. of their stock from the manufacturer, and the smaller ones from fifty to sixty per cent. Laces and linens are largely purchased of the manufacturer or of their agents, which is true equally of underwear, furs, hosiery, rugs, and books. Publicity, traveling salesmen and the mail order, combined with quantity-buying, have rapidly taken from the jobber the more important portion of the trade. Gents' furnishing goods are bought generally through the jobber, but the tendency is to buy from the manufacturer of special lines, and some well-known brands are sold through the agency plan; this is true espec-

ially of the better grade of hats. In the larger cities the manufacturer of collars, cuffs, and hats has his own stores for the retail and the wholesale trade.

Hardware and groceries are two important lines still largely controlled by the jobber. This is peculiarly the case of hardware for the reason that the stock is bought from so many factories and in such small quantities that the retailer cannot get on the jobber's list for most goods. This is also true of the grocery business, but not to the same degree.

By the above illustrations, which are typical, it is observed that the chain of direct sales begins with the manufacturer and involves the commission man, jobber, wholesaler, and retailer. The three primary steps, however, are from the manufacturer to the wholesaler, then to retailer and finally to the consumer. Before the days of extensive advertising the wholesaler, with his traveling salesman, commanded the vantage-point of distribution. He is an old landmark in the organization of distribution, and in former days was known as the merchant prince. His power was increased with the growth of the factory system, and he has gradually engaged in the selling of the factory output. The jobbing system of the older countries preceded the factory system, but in the United States it developed with it. A special class of business men were required

to organize the market. Gradually these organizations divided into wholesaling and retailing. Formerly through this system the output of factories was generally marketed, and the manufacturer was relieved of the trouble and anxiety of watching over an elaborately organized sales department. But the conditions already outlined are rapidly modifying this old institution.

As a result of this struggle for position in distribution, the manufacturer has in many instances established his business in the retail markets. This has been accomplished in some lines through the agency and in other lines through the chain of stores, managed from one central office. The advantage comes in buying stock in large quantities and distributing it among the several stores. The chain system is also employed by the manufacturer; it is the exclusive agency plan in a somewhat different form. The system has come into extended use in recent years, and fits well into some lines of business. Innumerable examples of the chain system could be cited varying in number from two to hundreds of stores. The history of the chain of stores indicates their continuous expansion. Their buying capacity affords the main reason for their growth, as these stores furnish in the retail market an outlet for vast quantities of goods. This is true especially of the great chain of department stores such as those

managed by Siegel, Wanamaker, Hartman, and Spiegel.

The effort to eliminate the jobber is apparent in all lines of distribution. In fact, in some instances it has been virtually accomplished so far as the better class of trade is concerned. The causes which have brought about this newer trend in distribution are universal in their application. We have already called attention to the fact that competition has generally narrowed the margin of profit for all interests. In other words, there is a minimum margin between the cost of production and the selling-price which must go to the selling interests to pay the selling costs and provide profits. The control of this margin has led to this readjustment of the distributing interests. But the control of the margin is not, however, the only element. There remains the manufacturer's interest in a large and constant outlet for his factory product, and to safeguard this interest the manufacturer has been led to revise his selling policy, even if he does not engage directly in selling.

These observations will appear more clearly if we illustrate them in a more specific way. Let us take first the manufacturer's point of view. In many lines his product is so protected by patents and trade-marks that competition is virtually eliminated except in so far as there may be competition with the trade-mark goods of similar

firms. In these cases he is usually vitally interested in the details of his selling policy. As a result the branch-office and agency plans are employed either separately or in combination. By controlling this sales department he accomplishes several things vital to the welfare of his business. He is in a position to push his own sales and to control prices. He controls his selling policy in all of its phases and prevents the cutting of prices. He has made himself independent of the jobber, and has through his own sales department and agencies secured a constant outlet for his output.

There is, however, a large quantity of goods not protected by patents or trade-marks, and the manufacturer of those goods must bear the brunt of competition in the jobbing market. While his goods may be of fair quality, there are many brands on the market which may be used effectively as substitutes. One year the jobber may place with a factory a large order which will compel the manufacturer to increase his plant; the next year the jobber demands a cut in prices, which, if not met, results in his placing the order with another factory. Thus the first manufacturer loses the very business which had caused him to make expensive extensions. It is this uncertainty which has compelled the manufacturer to protect himself in various ways.

The key to the present situation is quantity

buying. In order to protect himself, the manufacturer has made it possible for the retailer to buy with advantage directly of the factory. In other words, he has extended to the retailer privileges similar to those enjoyed by the jobber, provided he buys in sufficient quantity. The manufacturer fixes a wholesale quantity or jobber's list, and any dealer who buys in these quantities can secure the goods at the wholesale price. This enables the large retailer to pass over the jobber and buy his stock directly of the factory. In some instances, however, the manufacturer will sell only to the regular trade.

Wholesale or quantity buying grows naturally out of the factory system. It is a well-known principle that after an amount covering all costs has been manufactured, any additional increase augments rapidly the profits of the factory. In order to run the factory at full capacity, the manufacturer must not only have a constant outlet, but he must frequently offer special inducements to encourage quantity buying. He cannot afford to take the risk of depending alone upon the competition of the jobbing trade, because it means competition between the manufacturers. By making a price upon wholesale quantities open to all the trade, the manufacturer is in a more independent position.

In some cases, in order to secure these discounts for wholesale buying, it is necessary for the

dealer to get on the jobber's list. The jobber's list is fixed for each line of goods, and is determined either by a numerical or money standard. This standard will vary with the character and value of the commodity. In some lines this is controlled by powerful associations which determine the right of the dealer to enjoy this privilege. Again, in some lines the wholesaler is given an additional discount above that given to the retailer, which enables him to prosper, since he can then meet the manufacturer's discount, and induce the retailer to buy of him, and upon a large volume of business still secure a reasonable return for his efforts. But when this condition does not prevail, the jobber is at a grave disadvantage.

It will thus be seen that the jobber stands between two forces which are pushing him hard in the trade, and in some lines is virtually driven from the field. The manufacturer's desire to secure a position of independence, especially as to the wholesaler, has led to this policy of permitting the retailer to save the wholesaler's discounts by going directly to the factory. Quantity buying enables him to do this.

It must not, however, be inferred that the jobber has entirely lost his hold upon the trade. On the other hand, at present at least, he serves a considerable trade. As a general rule, his position is threatened in the high-class trade, and,

further, he is fast losing the trade of the large retailers. These buyers go to the factory. Each retailer attempts in his "anticipation orders" to load up to the demand. Naturally, in order to prevent overloading, he buys conservatively, and frequently is compelled to make additional purchases, and these "fill in orders" at present usually go to the jobber, and they aggregate often as high as 30 per cent. of the total business for the year. So long as the manufacturers will sell to the retailer only a quantity of goods of uniform type, the "fill in orders" must go to the jobber.

Again, the jobber at present controls the bulk of the trade of the small dealer, and especially that of the small cities and villages, or what is termed the country trade. This leaves him in possession of the trade of the small merchant, who cannot buy in sufficient quantity to secure the manufacturer's discount. Most of the country trade is of a lower grade.

This situation has grown up in recent years in most lines of trade. The manufacturer is carrying at present the accounts of innumerable retail stores, where formerly he carried the accounts of a limited number of jobbers. The danger from loss through bad credit under the old plan was much less than under the system of direct dealing with the retailer. The latter plan has been developed in a period of prosperity, but is yet to be tested in a period of business depression. So

long as consumption is large, the retailer can meet his bills during the discount periods. Expired time payments are not frequent. But periods of business depression, or limited consumption, are not unknown, and it is exceedingly doubtful whether the system of direct dealing with the retailer can stand during a period of depression. What would be the situation? The retailer would first feel the depression and would ask the manufacturer to tide him over. But he is not buying of one factory, but from many factories. It might easily happen that the manufacturer with the smallest order would proceed to make his collections and force the retailer into bankruptcy, which would in turn bring loss to all the remaining factories. This is a real danger to the manufacturer who carries the accounts of a large number of retailers, and it is very doubtful whether he could do this during times of business stress. It should be added, however, that the manufacturer is to-day more exacting in his collections than the jobber.

It is largely a matter of conjecture how the ruin of the retailer and loss to the manufacturer under the circumstances could be prevented. The system of direct dealing with the retailer could be abandoned, and a complete return to the jobber could be made, but this is the very thing that the manufacturer has been struggling to avoid. It has been the practise of the jobber in the past to

carry the accounts of the retailer, provided the latter would agree to buy from him the larger portion of his stock. In case of trouble, the jobber was directly interested in keeping the retailer in business, and consequently would guarantee his accounts and tide him over. He had too much at stake to permit another jobber who carried a small account with the retailer to force the latter into bankruptcy. By this plan of guaranteeing accounts the jobber has kept many retailers in certain lines under his control for the greater portion of their trade.

This plan of guaranteeing the accounts of the retailer might be adopted by the manufacturers. It would compel the organization of an association for this purpose. In this way the aggressive manufacturer could not force trouble, as he might under the present plan. It might also be possible to extend the credit clearing-house system to cover this class of credits, and in this way each manufacturer could bring his accounts with different retailers to the central office, and the financial standing of each retailer could be readily ascertained.

In New York City the beginnings of this system are already present in the case of foreign manufacturers. One firm, for instance, acts as the banker for a number of foreign manufacturers of different lines. The business is divided into departments for convenience, and certain

ones are assigned to wholesalers—silks to one and woolens and cottons to another. The guaranteeing firm assumes all risks and settles with the foreign manufacturer. The success of this plan suggests its further application.

Another plan that could be employed is credit insurance. Each retailer could be asked to have his accounts insured. This would bring about carefulness. It will be interesting to observe whether the system of dealing directly with the retailer can stand the stress of hard times. If the manufacturers can get together and guarantee the retailer against hasty action, all may go well; but if not, there will be nervous manufacturers and jobbers who will close in upon the retailer, causing not only a shrinkage of values, but a curtailment of the output such as would seriously affect the manufacturing interests.

There is one further observation that should be made at this point. The manufacturer may find the system of direct selling entirely too unwieldy for his sales organization and the risks too large in the end. Shrewd business men are not yet convinced that this will not ultimately prove true. In fact, in some lines of distribution, there is a slight turn of the tide back to the jobber. During the last few months the large packers have been returning to the jobbers. The manufacturer fears the large distributor. But there are advantages in dealing with the jobber, especially in

the guaranteeing of credits and the making of settlements. For this reason it is not at all unlikely that the small jobber will be favored by the manufacturer, particularly the jobber of groceries and provisions. By this plan the jobber is brought nearer the trade, and is still not strong enough to dictate to the manufacturer; but he is compelled to work effectively a small territory. He can also handle the problem of credits and collections with smaller loss to the trade. There are many facts to indicate that this plan will gain ground in the future.

XI

WHOLESALING AND RETAILING

In the foregoing chapter the principal features of the system of direct sales, and especially the methods of controlling the market and prices by the manufacturer and wholesaler, were presented. Consequently any extended discussion of wholesaling and retailing is unnecessary. It was shown that the manufacturer might employ the wholesaler and retailer to sell his output, or the retailer only, or he might sell directly to the consumer through a chain of retail stores, or the mail-order business.

It is our purpose now to examine in closer detail the organization and methods of wholesaling and retailing. While attempts have been made to eliminate the distributor, still, in many lines of business, he is recognized as indispensable. There are a large number of factories which cannot economically support an extensive sales department in widely scattered and distant markets. Besides, the business of manufacturing is quite distinct from that of distribution, both in organization and in function; so much so that it is a doubtful policy to combine the two functions under one management in most instances; it is

only under exceptional circumstances that this can be successfully done.

Generally the business of distribution is recognized as distinct from that of production and manufacturing. Distribution begins at the factory, farm, or mine. We are now to note the organization of those firms engaged primarily in the distribution of the factory output. Beginning with the factory, we find that frequently the important task is to dispose of the output in large quantities, and it is this fact that gives to wholesaling its special importance. The primary function of the jobber or wholesaler is to organize the market for the manufacturer. Often the large wholesale houses take the entire output of several factories. They buy in large quantities, and have their purchasing agents in all the principal markets. In the trade jobbing is virtually synonymous with wholesaling. However, jobbing is less inclusive, while wholesaling refers to the broader aspects of distribution. Still, they are essentially the same in organization and purpose.

The jobber or wholesaler exists in nearly all lines of trade, and stands between the producer and the consumer. The wholesale business has been greatly affected by consolidation, and by the establishment of retail stores; this is true especially where department stores have appeared. Here the retailer is in competition with the wholesaler, and in some instances has virtually driven

him from business, because the former can buy in such quantities as will enable him to get on the jobber's list. The large retail department stores carry enormous stocks, and can deal directly with the manufacturer with good results both to themselves and to their customers. Formerly a large capital was required, a fact which made the commission merchant necessary. This necessitated separate capital and buildings to bring the goods to the attention of the wholesaler. Two risks grew out of this—the manufacturer's and the commission man's risk. At present in some lines of trade the manufacturer is usually in closer touch with the retailer, and does not need to take the large risks of former days, or to employ the commission merchant to make his sales.

There are two classes of jobbing-houses—general and special. The latter largely predominates, although general wholesaling has increased in some instances; still, the wholesale business is virtually specialized. It is in the terms of the trade a one-line business. The scope of the one-line wholesale house is determined by the natural grouping of commodities. The trade recognizes the following lines of distribution as the basis of division and organization: dry-goods, groceries, clothing, boots and shoes, drugs, jewelry, hardware, millinery, music supplies, stationery and books, and machinery. This classification is arbitrary, and has been developed by the trade for

its convenience. Some of these lines are still more specialized, notably the dry-goods business. We find in the latter case houses handling only ready-made clothing, or collars and cuffs, or cotton, or woolen goods.

The advantages of confining the business to one line are many. The most significant is the mastery of the principles of distribution in one line; at least it leads to the consolidation of energy and capital. The volume of distribution in any one of the principal lines is sufficient to warrant the maintenance of large and carefully specialized departments. The danger lies in taking on other lines, which require other methods and policies. It multiplies the number of departments, introduces new problems and divides attention. Economy in investment, and particularly in management, seems to indicate the survival of the one-line wholesale house, although efforts have been made to eliminate the jobber, or to reduce at least the number of houses, through the consolidation of several lines of trade under one management. Both of these attempts have been successful, but especially the former, through the establishment of wholesale department stores in the large cities in connection with the retail business, which enables buying in such quantities that they can go directly to the manufacturer, and secure a substantial reduction in prices.

We have already noted the tendency to elimi-

nate the wholesaler in some lines of distribution. The most important gain is due to the fact that the goods can be made nearer to the time of delivery, and that the commission man, who acts as the agent of the merchant, is not compelled to find a jobber, who in turn has to search out the retailer. This condition applies especially to the dry-goods trade, novelties, and specialties. In agriculture the commission man is also a jobber, and buys directly from the local grain dealer. In some lines, such as fruits or vegetables, a jobber or commission man is necessary, since the product which he handles is perishable, and losses would result in most cases if the farmer were compelled to ship personally to customers in the city. The produce commission firm sells its stock to the retailer on short notice in order to prevent loss. In some cities co-operative companies have been formed to handle produce and other lines. These are organized and run directly by the farmers or producers, and have worked well in many instances.

Many firms do both a retail and jobbing business, and large manufacturing firms with branch houses scattered throughout the country often carry side lines. In this way the wholesaler, by taking on these side lines, accommodates his customers and increases his business. This mixed system of wholesaling is well illustrated in the agricultural implement business. At the main

distributing points of the principal farming sections the leading manufacturers of agricultural implements have established branch houses. The branch house is placed in charge of the business of the territory. Then the local agents in the majority of cases handle a large variety of farm implements, vehicles, hardware, and sundries as jobbing stock.

We may illustrate still further the organization of the wholesale business by noting some of the characteristics of the grocery business. This may be considered as a one-line wholesale business. In many respects is is one of the most intricate in organization and scope, for the reason that it includes so many different articles and so many different brands of the same goods. It is a large problem to assemble all the articles which are found in the warehouses of the wholesale grocer; they are brought together from distant lands, and under various circumstances. The magnitude of the business demands large capital, and great managing ability. Probably the largest wholesale grocery firm in the world is Sprague, Warner and Company of Chicago. In addition to this, Chicago has as many as twenty grocery firms doing a wholesale business exclusively.

The business is divided into departments. Among the principal ones are tea, dried fruit, flour, coffee and spices, baking-powder, refining and preserving, canned goods, salt, fish, cheese,

fruits, nuts, provisions and farinaceous goods, foreign and fancy groceries, cigars and tobaccos, and candy and sundries. In addition to these departments are found the purchasing, advertising, bookkeeping, and sales departments. At the head of each department is a manager, who has usually secured his place after a long experience, and after the demonstration of managing ability. In some instances the Chicago firms have employed these men from fifteen to twenty-five years. The general management of the wholesale grocery business is quite similar to that of the department store.

Often the wholesale grocer controls the output of factories which is delivered in packages under his trade-mark. In some instances he installs expensive plants for the purpose of preparing raw materials for the market, such as coffees and teas; In this way the wholesale house develops its grades and blends. Baking-powder and extracts are jobbed to a great extent, although some jobbing-houses prepare their own extracts. They also have refining and preserving departments. Canned goods are usually jobbed. Candy is often manufactured by the jobber. Sugar is also jobbed, and the large refineries have their representatives at the principal markets. It will thus be seen that the wholesale grocer is first a jobber and frequently a manufacturer. But this latter

business is insignificant when compared to his business as a wholesaler.

It will be observed that many houses have their own grades put up under the firm's label. For example, Sprague, Warner and Company employ the words "Richelieu," "Batavia," and "Ferndell" for their high-class goods. These brands cover the same goods in order to give exclusive selling rights to different local grocery firms in the same city. In this way the brand becomes known to the public as a standard of excellence. The wholesale business is carried on almost exclusively with the retail grocer, and no attempt is made to reach the consumer directly. The mail-order business is used primarily to fill the orders of the retail grocer, who knows exactly what he wants, and does not care to wait for the visits of traveling salesmen. The two most important departments of the jobbing-house are the purchasing and sales department. The other departments are of great importance, but, outside of the advertising department, they are not considered as creative, but exist merely for business efficiency and system. Considerable specialization is found in the organization of the larger jobbing-houses.

The wholesale house usually employs three methods in reaching the retailer. The most general one is through the traveling salesman, who has a certain territory, which is covered at regular

intervals. The second method is through the catalogue of prices and descriptions of articles, which the retailer, and especially the country merchant, uses in ordering through the mails. Inducements are offered to the retailer for the purpose of increasing trade. The mail-order plan is exclusively employed in the grocery business only by one or two firms. Finally, most firms employ the combination of the two systems.

In the foregoing discussion we have been dealing with the general features of the wholesale business. We have considered the wholesale firm as conducting its business at some large distributing market, but most firms are not content to wait for business to come to them, but rather, through well-known methods, they seek to carry their business to the retailer and the consumer. In order to accomplish this, the wholesaler frequently adopts a policy of decentralization. It is similar to the policy of the manufacturer when he deals directly with the retailer or consumer. The methods were presented in the foregoing chapter.

It is customary for the jobber to open up a central or home office at the important distributing market. Some cities have become known in the trade as principal markets. In most instances New York City holds a leading position, and is a favorite place for the location of the home or central office; Philadelphia, Boston, Chicago, St.

Louis, and other cities are also known as leading distributing markets for some lines.

It will thus be seen that the district system, with its branch office, is most successful when the volume of business is large and widely distributed, and when the element of direct sales is prominent. It is most successfully employed in those lines where consolidation has reduced the number of distributors, or where the article is protected by patent rights.

The final step in distribution is retailing. The retailer stands near the consumer, and his task is to organize the consumer's market. His business is local, and his relationship with the consuming public is largely personal. The retailer is the local merchant, or shop-keeper. In law, a dealer is one who buys and sells an article without change in its condition, and the term is generally used as synonymous with retailing, although it has a somewhat broader meaning in the trade.

The stock leaves the shelves of the retailer through direct selling. There is one principle of supreme importance in distribution: a commodity well bought is well sold, and this is especially true of retailing, for the reason that personal tastes must be satisfied. It is at this stage of distribution that custom and vogue are forcibly felt. Retailing consists of three operations, which, if well performed, bring success, viz., careful buying, a careful arrangement of stock, and a careful

and courteous treatment of the customer. It is in the buying that we find the surest test of the judgment of the retailer and of his knowledge of the wholesale market, as well as the demands of the local trade. Modern advertising has greatly minimized the dangers of over-stocking for the reason that the demand is created before purchases are made. In purchasing stock, the successful retailer has his attention fastened directly upon the requirements of his customers.

It has already been noted that wholesaling is either general or special. This is likewise true of retailing. It was further observed that special jobbing was the rule. This is also true of retailing, but probably not to the same degree. The general retail store is still dominant in the smaller villages and cities. But as we pass to the larger cities, the special one-line store grows in number, and virtually predominates. The most notable exception is the department store, which in many instances is a general retail store highly specialized in organization.

There are two primary considerations controlling the consumer's buying. One is the quality and style, and the other is the price of the commodity. The first, in the long run, controls in the majority of cases. The customer is willing to pay for quality well guaranteed, and for this reason the one-line, or special, stores are profitable, and continue as the favorite form of retailing

outside of the large cities, and even in these they seem firmly established in the confidence of the public. The department store has proven to be the most economical mode of general retailing, and the strongest competitor of the one-line store.

There are many sound business reasons for the wide use of the special store as a form of retailing. It opens up an opportunity for a reasonable income upon a limited investment. It affords an opportunity for the exercise of special tastes and talents for management. Attention is concentrated, instead of being scattered over several lines more or less remotely related. It is easier to build up and hold trade. It fits well into the business habits of smaller communities, for the reason that the customer, as a rule, desires to distribute his trade among several retailers. He desires to buy his shoes at one place and his groceries at another store. The one-line retail store also fits into the organization of wholesaling, of which it must be considered an organic part, since we have found that wholesaling is carried on in the main as a one-line business. The most significant feature of the one-line retail store as a business institution lies in its cultivation of higher standards in the selection of stock, as well as in its creation of a wholesome rivalry among a class of independent retail specialists.

A casual canvass of the retail stores of any community will serve to illustrate the truth of

these observations. About the only one-line store that has been successful in competition with the department store is the one cultivating a high-class trade. In some lines of business the one-line store is virtually the rule. This is true particularly of hardware, boots and shoes, dry-goods, drugs, groceries, machinery, musical instruments, and supplies, clothing, etc. In some instances these are still further specialized, as in the case of the clothing business. The old general store fits into the business activity of small communities, and survives to-day at the country cross-roads and villages, where special trading cannot be successfully carried on because of the small volume of business; but even here evidences of specialization are seen.

The problems of retailing in the larger cities are so different from those of the smaller ones, that in most lines of trade the city and country retail stores stand in separate classes. The city retail trade is influenced by the large department store, and through the concentration of business generally. The tastes of the customers are more highly cultivated, and trade is conducted on a more liberal scale. Style and vogue are also more conspicuous in the city markets.

The one-line retail store is generally looked upon by the trade as being practically identical with what is termed the small store. It stands almost in a class by itself. It must not, however,

be inferred that the one-line store may not be divided into departments. In fact, in the larger cities this is the general rule of organization. It follows from the volume of business, which requires a separation into departments in order to secure efficiency in buying and selling.

There are obvious dangers connected with retailing. One of the greatest of these is overstocking. It is easy for a practised and skilled traveling salesman to present engaging arguments in favor of his line. The retailer is likely to be persuaded "to take a case" with the result that often the goods must be sold at a loss unless the retailer keeps in close touch with the demands of his customer, and buys accordingly. It is scarcely the function of the retailer to create wants, but rather to buy for wants that are stable and felt. The larger capital, experience, and opportunities of the wholesaler and manufacturer fix upon them the responsibility for the creation of wants.

The general experience of retailing shows that in the long run a successful business can be built up alone on the policy of giving the best values possible. The price is not the main consideration. There is an old trade proverb that quality is remembered long after price is forgotten. It is at this point that a considerable reliance must be placed upon the reputation of the wholesale firm.

The marking of prices opens up a divergent

practise. Some dealers mark by symbols, and others in plain figures. The former is used to place the selling and cost price side by side for the guidance of the clerk. The general feeling seems to favor the open-price system, because it cultivates in the end the confidence of the customer in fair treatment. As a general rule, the best and largest trade will be secured through the one-price system. There are two ways of offering reduced prices: first, to individual customers, and, second, through advertised bargains as leaders, or baits. The first is a dangerous method of attempting to build up and hold trade, and the second is also a doubtful policy. This is the age of the bargain-counter. But bargains do not hold trade. It is a species of business warfare, and cultivates the chronic bargain-hunter who has no fixed place for trading, but follows the price-cutter. There is a special side to retailing, which goes back to courteous treatment and fair values at open fixed prices. Location may be an important factor in retailing, but individual taste in decorative fixtures and shop displays appeals universally to the public. Prompt and polite service will in the end select and hold trade, which will not be turned away by the flattery of the bargain-counter. The carefully managed one-line store exists because there is a large body of customers in every community which desires

the one-price policy, combined with substantial values.

In order to avoid the necessity of cutting prices, a policy of quick sales and small profits is advocated. This is at least the educational argument of the retailer, and while it is sound in theory, the practise is divergent. Domestic and staple goods, which are popular-priced, are usually sold on this basis, but it is not the case with high-grade goods and special wares. This is the basic feature of the policy of the department store. In order to hold the trade, the small one-line store must guard well the selection of stock, for generally it will be sought out for special values and styles, but particularly the latter. The rapidity of the "turnover" determines successful distribution. The number of "turnovers" may be increased through advertising, fair values with fair prices, and courteous treatment of customers. The number of "turnovers" varies with the conditions and lines of trade. Because styles change with the change of seasons, quick sales with small profits generally lead to a greater volume of business.

One special feature of the retail business should be noted. The retailer may make his order in the following ways. They may be made of the traveling salesman, by mail, or by personal visits to the wholesale markets. Formerly it was a favorite practise of the wholesaler to entertain

the country merchant on his annual visit to the wholesale market in search of stock. These personal visits were specially valuable to those merchants whose business is affected by changing styles; also it possessed some advertising value. The announcement of such a visit carried with it the thought that the stock was personally, and, consequently, better selected. New York and Boston were visited for woolen and silk, Philadelphia for carpets and rugs, and New York for notions, novelties, and clothing. But the more recent trend toward direct selling has changed the situation so that these visits are now less frequently made. In fact, in some lines they are now rarely made. The traveling salesmen, together with publicity and the mail-order system, have rendered these visits unnecessary in most cases.

The organization of the retail business is quite simple. The most important consideration is the purchasing and selling policy. In addition to the salesman, the only necessary employees are those in charge of the books. A great many features of retailing are closely related to wholesaling. A most important function of the retailer is to meet the consuming public at the counters on friendly terms. It is the function of the manufacturer and the wholesaler to assist the retailer in every possible way to create and stimulate wants, and to direct the attention of the consumer to the shop where these may be satisfied.

XII

TRAVELING SALESMANSHIP AND THE MAIL-ORDER BUSINESS

There are some important phases of the market which deserve a more special treatment than could be given in the chapter on wholesaling and retailing. They have been frequently alluded to in the foregoing discussions. Among these are traveling salesmanship, the mail-order business, credits and collections, and advertising. These have an especial bearing upon distribution. In this chapter we shall take up the function and organization of traveling salesmen and the mail-order business, not because they are so closely allied as to require treatment together, but because the limits of space prevent any extended separate discussion of them.

Before the days of extended publicity it was customary for the manufacturer and wholesaler to employ almost exclusively road-men to sell their goods. While this form of salesmanship is still extensively used, it has, however, been materially curtailed in many ways. One of the most forceful arguments for the consolidation of industries is the saving which results from reducing the number of traveling salesmen, if not

wholly eliminating them. For instance, the organization of United States Steel Corporation retired many hundreds of road-men employed by the competing plants. The testimony given before the Industrial Commission shows conclusively that a material saving has accrued to trusts and combinations on this item of expense alone. Although these conditions have in many instances reduced the number of road-men, still, in many lines of distribution they are yet indispensable.

A traveling salesman is the accredited representative of a business firm in the exploitation of distant markets. He may represent a manufacturer or distributor. In many instances the manufacturer contracts his output to one or more jobbers, who in turn undertake the selling. These houses then employ, in connection with their sales department, and in close relation to their advertising department, a crew of road-men to visit certain localities and markets to sell their goods. This is the direct method of reaching the retail trade.

There are two classes of salesmen. One class is the clerk at the counter, who meets the customer personally, and is the last link in distribution. The second class is the traveling salesman, or road-man, who is engaged in exploiting the merits of commodities in the wholesale and retail markets. They may consist of an elaborately or-

ganized force, penetrating communities far from the central office. With the wide growth of distributive activities the traveling salesman becomes an important agent in the work of publicity, and while his work is distinct from advertising, nevertheless it is closely allied to it.

Road-men are divided into two classes—general and special. The general road-men carry all the lines sold by one concern or by several firms. The larger wholesale houses have their general traveling salesmen, who are sent into the territory where small markets abound, and form the principal reliance of the house in maintaining a regular trade. They visit the smaller retail stores which buy a large variety, or do not deal in special wares in quantities which would warrant the visit of special salesmen. The general salesmen "make" these towns at regular intervals.

The special salesmen are found with those firms carrying a special line of goods whose value is large and frequently fluctuate with the seasons. It is customary for the most progressive retail merchants to buy upon inspection. This is done by going to the larger distributing markets, or by inspecting the samples of the traveling salesman. The practise of retail merchants of visiting the wholesale markets to lay in their stock is rapidly passing away. These visits are made unnecessary by the use of traveling salesmen. Often a special salesman is able to sell where one em-

ployed in general work would fail, because of the fact that the former is usually better qualified. A great variety of dry-goods is sold through special salesmen, who visit their customers in season; they "make" the larger towns, and visit only the more progressive merchants. Their field is limited both in territory and commodities, as well as in the number of merchants visited.

The road-men operate from the central office or its branches. The sales manager directs his office and his entire corps of salesmen, while the sales manager of the branch office is virtually in charge of an assigned territory. It is customary to place over each territory a manager for the supervision of the salesmen. The duties of the manager of the road-men are important. He must, in the first place, be a man of good business ability and a keen judge of men. He assists in making prices, because he knows the conditions of the market. In this way the salesmen are directly or indirectly controlled from the home office, but in case the trade expands over a wide territory, branch offices are established. A warehouse is frequently established in connection with these branch offices.

One of the first problems of the sales manager, after the selection of his salesmen, is to divide the territory so that it can be covered most expeditiously and economically. A number of considerations determine this division of territory,

the more important of which are the systems of transportation, number of retail stores, and the line of goods. The blocking out of the territory is done at the home office or at the branch office. The sales department seeks to meet the customer at regular intervals, and as often as the business warrants. This will obviously vary with the line carried. Transportation naturally controls in the first instance. But the size of the territory will be determined by the number of establishments to be visited. Where the territory is densely populated naturally the block is small.

Some of the larger distributors pursue the policy of meeting their customers once every week, especially in the larger towns. This is the practise of the larger wholesale grocery houses. The block expands with the longer intervals of the visit. Each salesman is usually assigned to a given route or block. This plan has its advantages, because it enables the road-men to make a careful study of the needs of his territory and to cultivate the good will of the customer. In some instances the salesmen are grouped into crews under the direction of a foreman. This is especially true of the book-canvassing business. Preliminary courses of training are frequently required of salesmen before they go on the road. In this way they become acquainted with the nature of the articles, the favorable arguments as well as the objections that must be met. This

plan is followed by those companies that deal largely with the individual.

Three systems are used by road-men in making their territory: the regular-trip system, the regular district special trip system, and the branch-office system. The first system is the most common, although the second has a large place in distribution. The last system is employed in those lines where the goods must be brought closer to the customer through the means of warehouses than is possible by operating from the home office only.

Before the salesman leaves the office a list of customers is prepared for each town. The standing of each customer is carefully examined. The samples are then prepared by men especially employed for this purpose, and marked by the heads of the various departments. Before the road-man leaves the home office, he must be thoroughly posted on the entire line he carries. His method of getting business is his own. The good salesman never truckles for orders; honor and merit are to him valuable assets.

The duties of salesmen often are more than selling goods. They must sell to persons of good credit, and avoid over-selling to those of slender credit. While the orders are finally passed upon by the credit department, still, the road-man can frequently save the office annoyance by exercising judgment in taking orders. In

addition, the road-man can render valuable service to his department by acquainting it with the conditions of the trade of his territory. He can report the changes in demand, the opening up of new stores, the nature of competition, and numerous other matters of great importance to his house.

The method of compensating road-men is important. Three methods are usually employed —the salary, commission, and a combination of salary and commission. The salesmen are employed in most cases under a contract which states carefully the conditions, duties, salary, expenses, etc. It generally runs for one year. In some instances no formal written contract is drawn, but the better houses consider this bad policy. The first general provision is that the salesman shall devote his time and energies to the interests of the firm.

Various provisions in regard to expenses are frequently incorporated. Some firms carefully look after the expense account of their salesmen, while other firms are very liberal in this respect. There is, however, no general rule governing expenses, but in most cases itemized statements are required. The Traveler's Report Book is a convenient form for reporting these as well as other facts to the office. It has been found by the best houses that it is a wise policy to fix expenses, and they have generally gone over to this

other system. The liberality of the house as to expenses is governed quite largely by the margin of profit and the character of the trade. The best houses require their road-men to travel well and to frequent the best hotels. Municipal supply houses allow liberal expenses to their road-men, because they sell on a wide margin of profit and deal with city officers, who must often be expensively entertained.

Where the firm does not require the full services of the salesman, he is usually employed on a commission basis. The goods of several houses may be carried in this way by one salesman. This method is employed by the smaller manufacturers and jobbers. But the tendency is for the smaller manufacturer to turn over his selling to the wholesale distributor, who in turn has his regular salesman. Where the commission plan is followed, the salesman usually pays his own expenses. Where the combination of salary and commission is used, the latter begins after the sales have aggregated a given amount. This plan is obviously intended to spur on the salesman, and is more generally employed by the larger manufacturers and wholesale houses.

By way of illustrating the methods of compensation, we may assume that the salesman has contracted on a salary basis with a commission feature. The guaranteed salary is usually from $1,000 to $1,500. He is then required to make

sales to a given amount before his commission begins. This amount may be fixed at $20,000, and the commission increases with the amount of the sales. The profit system is also sometimes used, whereby the salesman shares in the profits of his sales.

The selection of the salesman is most important, because they are the accredited representatives of the house to the trade. The firm is judged by the character of its salesmen quite as much by its goods. If the salesman bears the traits of honesty and fairness, the house has gained. It is impossible to forecast the success of a salesman, for the qualities of the successful salesman cannot be easily analyzed. His power of persuasion is personal. By meeting his customers from year to year, he comes to know their wants, and methods of business, and very frequently they depend upon him for advice concerning the newer trend in styles and in demand.

The control of the salesman by the sales manager cannot be put into definite terms. It is the result of business tact and generalship. Many of the details of control have, however, been systematized. In the first place, most houses require a daily, or at least a weekly report, but the kind of information sought will vary naturally with the business. The conditions of the trade, expenses, amount of sales, and other matters are items of interest to the sales manager. The

sales manager is in daily touch with his road-men. The notices of intended visits are sent to the customer in advance by the salesmen or by the central office. Many houses place in the central office a map of the sales territory, on which the position of each salesman is marked by colored tacks. Thus the house can know at a glance where each road-man is at a given time. In the same way the conditions of the trade may be indicated.

Another important service sometimes left to road-men is the collection of bills. Most houses, however, have a separate department for this work, and do not permit salesmen to make settlements. These houses have a corps of collectors who make the territory and adjust accounts. This practise is especially employed where the retailer is an agent. The prevailing method is to make settlements by direct remittance to the home office upon the presentation of a statement. Some of the hardware houses, however, permit payment to their road-men after a statement has been sent out by the home office, and some wholesale grocers employ this plan exclusively. The statement is sent to the salesman who takes off the discount for cash. The ledger method is also employed. It consists of two small ledgers, one always in the hands of the salesman, while the other is kept at the home office. Each ledger is for a definite territory, and while one is being used the other

is being posted. In the case of direct collections the salesmen are required to furnish bonds from the regular bonding companies, for the reason that these are rigid in prosecution.

This brief account of the organization of the road-men will serve to bring out some of the conditions of their relationship to the house and the trade. While their operations have been somewhat restricted through the growth of advertising, and consolidation, still, they must be considered an important adjunct to distribution. In the sale of staple goods such as groceries, clothing, hardware, etc., the traveling salesman finds his best field. These goods are bought in considerable quantities, and as the tendency is more and more to buying upon the inspection of samples, the hold of the road-men upon the trade is increased.

An important phase of the mercantile activity of recent years is the growth of the mail-order business. Local merchants have for a long time relied upon correspondence to replenish their stock, but it is not until quite recently that any systematic effort has been made to sell directly to the customer upon orders through the mails. Some of the business reasons which resulted in the organization of trusts, have also suggested the development of the mail-order houses. This is another feature of the plan to cut out the middleman, and especially the country merchant from

the chain of distribution. The growth of the mail-order business is natural and logical. Improved transportation and the extension of the mail service made it easy to secure samples from the city merchants and to make shipments. These orders were cumulative, and suggested the establishment of separate mail-order departments, which led finally to the organization of firms for a mail-order business alone.

Some cities are especially well located for this business, but none are more favored in this respect than Chicago. It is the distributing point of a large populous agricultural area, filled with many villages and small cities, which are connected with it by a splendid system of transportation. Consequently it is no surprise to find operating from Chicago two of the largest mail-order houses in the mercantile business. The combined business of all of the mail-order houses of Chicago is estimated to be nearly $100,000,000 annually.

In order to convey some idea of the size of some of these stores, a few statistics will not be out of place. The two leading houses are Sears, Roebuck & Co. and Montgomery, Ward & Co. These are retail mail-order houses. In addition, several firms conduct a wholesale mail-order business, and many city stores have mail-order departments. Various facts indicate the size and complicated organization of the mail-order houses.

The larger houses employ from 3,000 to 5,000 clerks to handle the correspondence, to fill orders, and to look after the packing, routing, and shipping. The average daily orders are from 15,000 to 18,000, and the daily holiday trade reaches 25,000 to 30,000 orders. The postage and express charges amount to several thousand dollars daily. The floor and warehouse space required to carry the stock is enormous. In fact, the central buildings are essentially warehouses, since few goods are sold directly to the consumer over the counter. The best houses make it a practise not to sell to city customers, and even instruct the floor clerks to inquire of each person entering the store whether or not he is from the country before making a sale; they are organized for the country trade.

The mail-order business rests upon publicity in its various forms. Aside from a limited newspaper advertising, their main dependence is upon the circulars and catalogues. On account of the feeling of the country merchants against the mail-order houses, the country newspapers are reluctant to carry the advertising of these houses. For this reason they must depend upon mailing-lists secured in various ways for the distribution of catalogues and special circulars.

The preparation of the catalogues is an arduous task. There is first and most important the general catalogue. This covers the general lines

which are staple and in constant demand. Since these stores assume to sell any article upon the market, this catalogue expands into a larger volume, and some contain descriptions and price-lists for as many as 70,000 articles. In addition, special circulars, booklets and samples are sent for the seasonal trade.

The importance of the catalogue and circulars cannot be overestimated. They must concisely, accurately, and truthfully describe each article. The catalogue is the silent salesman, and goes into the homes, and a leisurely search for articles is possible. Wherever the catalogue goes the store goes, and the post-office department is made the agency for delivery.

The mail-order business is based, first, upon a systematic organization, and, second, upon the delivery of the orders in a satisfactory condition at low prices. The carefulness with which the orders are filled is, in fact, the basis of a successful business. In this way the trade is not only made permanent, but each customer becomes a sales agent among his neighbors. Country customers seek plain goods at low prices. The same arguments of economy are urged for the mail-order house that are urged for the city department store. The latter is an aggregate of special retail stores, and in the same way the mail-order house is an aggregate of country retail stores.

For this reason it is undoubtedly true that

these houses can sell the goods to the consumer at a price below that of the country merchant. The large volume of trade increases their purchasing power. Again, the country retailer's profits are eliminated, and where the factory sells through the mails both the jobber's and retailer's profits are also eliminated. The expenses of the mail-order houses are advertising, catalogues, samples, postage, freight, and express charges, salaries of the clerical force, and the fixed charges upon the investment in buildings. But the aggregate sales of these houses is so large that their expenses are proportionately less than they would be were the same volume of business done through the ordinary channels of trade. The stock is bought directly of the factory in wholesale quantities. Consequently they buy cheaply. The country customer cares little for style, but he seeks substantial goods at low prices. Great stress is laid upon the saving of this system to the customer, as well as the great range of articles offered. In most cases better rates are secured by the mail-order house than could be obtained by the local merchant. The freight or postage thus becomes a small item, and as a result the country customer secures his goods at city prices. There are no profits for the middleman, except those of the mail-order house. Again, the business is organized on a cash basis, which enables a further reduction of charges.

In order to carry forward this enormous work, great attention must be given to organization. The establishment is divided into departments, similar to those stores doing a regular city retail business. The essential difference lies in the fact that the business is done through the agency of the mails, express and freight, which necessitates an elaborate organization to do the work rapidly and accurately. The surrounding country is divided into districts, according to the system so generally employed by all large houses. Essentially the same departments exist that are found in the regular department stores. The relation of the house to the manufacturer is likewise the same as other department stores, and differs only in detail. The essential differences lie in the contact with the trade. The relationship of the regular retail store with the trade is close and personal. The personality of the clerk is vital. With the mail-order house the relationship is not so personal, and the appeal must be based exclusively upon price and fair dealing.

While the mail-order business possesses great possibilities in scope and volume, and has taken away some trade from the country merchant, it cannot, however, be considered a serious menace to him. Through it he will be urged to cultivate better methods, and to make a more careful selection of stock. The only serious menace lies in the cut of prices, due to the fact that the mail-

order business is designed to eliminate the retailer, and that the business is done upon a cash basis. But the country retailer can meet this situation to some extent by buying of the manufacturer, thereby saving the wholesaler's profits. Furthermore, the latter can rely upon the fact that, all things being equal, the customer prefers to buy after a personal inspection of the article rather than by samples, and that he prefers often to pay a higher price for this privilege. This is illustrated in the survival and growth of the high-class, one-line retail shop in competition with the department store. The amount of the purchases of any one customer through the mail-order is generally small as compared with the total purchases from the country merchant. The rapid growth of the mail-order business must be accounted for on the ground of large business efficiency and economy, and where it is conducted on a large scale, it has proven an economic method of buying from the point of view of the customer. However, it should be added that the advantages to the consumer appear when a considerable quantity of any article is purchased. Doubtless these same reductions in price could be secured at the home market by buying in quantity. Again, the mail-order house does not exchange goods, which is so generally the case when they are bought of the local merchant.

In the aggregate, the mail-order business is

enormous, and is rapidly increasing. This development is in harmony with the tendency of trade everywhere to cut out as many of the intermediate steps as possible between the producer, manufacturer, and consumer. Through the aid of the city daily and the low-priced magazine the mail-order plan is widely advertised. Recent years have produced some far-reaching changes in the organization of distribution. Not the least important of these is the development of the mail-order business.

Distance is no barrier to the extent of the business, and with the rapid growth of the mail delivery the country districts can be more systematically exploited. It is to the country trade that the appeal is made, and, in fact, some of the large stores will not sell knowingly to the city customer. The mail-order house is a great clearing institution for the country business. It is shipping by mail. About seventy-five per cent. of the trade comes from the farming communities.

We have taken the point of view of the mail-order houses, but from the point of view of the country merchant there are certain features of the system which endanger his local trade. From the point of view of the consumer, however, an outside market is open to him, offering a larger range of articles of fair value at lower prices. Upon reflection, it will be found that the farming communities sell the bulk of their products in the

larger city markets. To these go by far the largest percentage of the grain and live stock. For that reason there is some business justice in the farmer going to the city markets for merchandise. But we are not concerned with the ethics of the market or with sound public policy. It is sufficient to observe that the mail-order business would not have assumed its present-day proportions, or have before it a future of so much promise, if good and substantial business reasons did not prompt the rural customer to seek the best market. It is purely a question of business. It is one of the price and the quality of the goods, and the country customer is entitled to buy in the best markets.

XIII

ADVERTISING

During the last few years advertising has grown to immense proportions. In various forms it has been a feature of the business activity of all times and places. Naturally, the methods of advertising will depend upon the nature and methods of industrial efforts. In a primitive business community the methods of publicity are simple, and largely by word of mouth and crude displays, but in our complicated industrial system advertising assumes varied and artistic forms.

Advertising is an outgrowth of the desire of the producer and distributor to extend their trade. If the customers are near at hand, the form of publicity will be different from that employed where they are scattered over a continent. The methods of advertising are, therefore, the outgrowth of the relationship existing between the manufacturer, distributor, and buyer. In our modern industrial system the manufacturer is widely separated from the consumer, with whom he naturally endeavors to establish a friendly relationship. He is normally interested in the extension of his business by cultivating new territories, or interesting new customers in his commodities.

Formerly it was the custom of the merchant to display his wares in the market-place, and to make their qualities known at the gates of cities; but these simple methods have been supplanted by printed advertising. It was not, however, until late in the seventeenth century that advertising in periodicals was first introduced. Commercial advertising did not appear until about 1688, and the first newspaper advertisement in the United States appeared in the *Boston News Letter* of 1704. The recent growth of advertising in the United States is strikingly shown by the fact that *Harper's Weekly* inserted its first advertisement in 1864; since that time the space devoted to publicity has increased enormously.

The development of modern advertising may be briefly indicated by a few statistics. At the beginning of the latter half of the nineteenth century there were scarcely any periodicals in the United States carrying advertising; to-day there are 20,000. These media have come into existence, not so much because of the demand of the reading public, as on account of the splendid profits to the publisher from advertising. This is still further shown by the fact that the average advertising receipts in 1900 showed a gain of fourteen per cent. in ten years, while the average receipts from subscriptions and sales showed a decrease for the same period. This is due particularly to the constant reduction of the price of

magazines and daily papers in order to extend their circulation, so that the rates for advertising space might be increased. As a result, the circulation of newspapers and magazines has, roughly, increased to 8,163,000 in 1900; the circulation has doubled every ten years.

Naturally, the great advertising centers will be found in those sections where industry is highly organized, and the country thickly populated. For instance in the State of New York there was spent in 1900 $25,000,000 in advertising; in Pennsylvania, $10,000,000; Illinois, $9,000,000; and Massachusetts, $6,000,000; and in the West the same ratio holds good. These figures do not include the vast amount of money put into circulars, pamphlets, bill-boards, and other forms of out-door advertising.

It has been estimated that the total annual outlay in the United States is about $600,000,000. This is one-half of the value of the annual corn crop, and twice the value of the wheat crop. Not many years ago, if a few hundred dollars were spent in advertising, it was considered a reckless venture; but to-day fortunes are spent annually by manufacturers and distributors of widely consumed goods. For instance, one firm distributed 25,000,000 almanacs in one year. It is asserted that Ayer's spends $600,000 annually in advertising his medicines. It is also asserted that the manufacturers of the Royal Baking

Powder spend about the same sum annually. The first important advertisers were the owners of medicines, and it was through their efforts that the value of publicity was demonstrated. The growth of advertising is doubtless due to a better judgment of the public in selecting goods, the growing wants of the consumer, and the prevailing conditions of buying and selling where the producer and consumer are widely separated.

There is a well-recognized relationship between advertising rates and circulation. The quantity and quality of circulation are the values that the advertising medium has to offer, and nothing else; the right to follow this circulation is what the advertiser purchases. To use space effectively is the function of the advertiser. The tendency is, however, for the advertising rate to increase, and for the subscription price to decrease, or to remain stationary. Advertising rates have probably increased more than one hundred per cent. during the last two decades, and many instances might be cited of the large prices commanded by leading journals for advertising space. It is said that the *Ladies' Home Journal,* with a circulation of over a million, has secured long-time contracts for the last cover-page at something more than $4,000 per issue. When compared, however, with the number of readers of this magazine, the cost is very much less to the advertiser than if the same number of persons were reached through the

mails. On account of the enormous expenditure required for advertising, there has naturally followed a keener desire to use advertising space effectively.

As already stated, the price of advertising space is determined by circulation and the class of readers. The circulation furnishes a tangible basis for fixing the price. It is, however, not infallible. The rate is usually fixed at so much per thousand of circulation, with a scale of prices for increasing and decreasing circulation. While some general rules governing the price may be laid down, it remains true that advertising space is bought and sold on the market, and prices fluctuate as do those of other commodities; still, there is a strong tendency toward fixed rates upon an equitable basis.

The advertising movement has devloped special advertising agencies. These are the outgrowth of a scientific interest in advertising, stimulated by the profits of the business. The agency is an organization of men competent to select suitable advertising media, create ideas for the copy and make illustrations, attend to all the details of execution, make collections and settlements, and, in short, to co-operate with the advertiser in conceiving, developing, and perfecting all the features of the advertising campaign. In this way the recklessness of former years has been largely

eliminated, and the business has been placed on a more careful and permanent basis.

The rapid rise of these agencies has followed the demand for a more businesslike treatment of advertising. Out of a period of reckless, sporadic, and haphazard advertising there is rapidly emerging an era of systematic effort. About sixty advertising agencies in the United States have been accorded recognition, and given a commercial rating. They serve a legitimate function in business. The more recent development of the market has necessitated different advertising methods. The customer desires to know the quality and cost of goods. The problem, then, for the manufacturer and distributor is to get this information effectively before the public—the advertising agency assists in the solution of this problem.

Formerly advertising was considered a questionable business venture, but to-day it is looked upon as a business necessity. It was once ineffective and experimental; and it is estimated that seventy-five per cent. of the early advertising did not pay. To-day it is becoming more and more effective. It has been found that its influence over business is far-reaching, and that successful advertising rests upon stable business conditions. In order to expend effectively an appropriation for publicity, some adequate notion of the principles of advertising must precede the

campaign. The view long prevailed that advertising was a game of chance, but this view has been superseded by a feeling that system is the basis of success in advertising as in other undertakings.

The view is held by many that the enormous expenditures for publicity constitute an unnecessary economic waste. It is often treated from the social point of view as a waste incident to competition. This assertion is doubtless a partial truth, but it is based mainly upon the view that advertising is largely to convey information and does not sufficiently emphasize its bearing upon the creation of business.

Advertising is generally viewed as a creative business force. It is concerned primarily with the sale of a particular commodity, and secondarily with enlarging the demand for this commodity by suggesting new uses for it. The manufacturer of cereal foods is engaged, first, in pushing his brands, and second in suggesting new recipes and ways for serving them. Naturally the manufacturer, wholesaler, and retailer are mutually interested, but the manufacturer's interest is especially prominent, and is doubtless a primary cause for the growth of advertising in recent years. He desires to create a demand for his wares which will be felt so strongly that the retailer and wholesaler must buy of him. Such a demand is his chief weapon in his struggle for

independence against the wholesaler and retailer. The decreasing margin of profit, the growing power of the traveling salesman, and the independence of the wholesaler and retailer were rapidly placing the manufacturer in a dangerous position. He began to realize that it was unsafe. He saw his business largely controlled by the distributor, who was not vitally interested in his particular wares, and who was willing to transfer his business from manufacturer to manufacturer, according to favorable inducements and fluctuating prices. Any break in the link between the consumer and himself meant disaster to him. As a result, it became necessary to cultivate more closely the good will of the consumer. His most effective weapon was advertising. He began to advertise and develop his trade-mark. The customer, in turn, sought his goods at the counters of the retailer, who, in turn, made the demands of the consumer known at the wholesale markets. The result is a larger independence on the part of the manufacturer through the creation of a normal demand for his goods which cannot be disregarded by the distributor. There has therefore been in the last few years a studied effort to bring the consumer and the commodity into closer relationship.

Advertising adds in this way new values to commodities by utilizing wants already created, or in process of creation. Commodities have

varying values, for the reason that the conditions of life are constantly changing, and tastes are being modified. While the manufacturer is engaged in the production of goods, and the middleman, in their distribution, there must be some effective agency engaged in attracting and holding the attention of the buyer. This is the function of advertising. It is the power of persuasion. Advertising in the business world is a great propelling force. It induces the buyer to accept particular goods which are offered for sale, and this gives new value to goods and services.

At one time advertising was largely a method of information. It was a statement of prices, a time-table, or a schedule, and did not usually contain an argument for the commodity. But the more recent view is that advertising is creative, and that its object is to stimulate and arouse new desires. It presents an argument and develops the merits of a given commodity, and sends it abroad to awaken a desire to possess this commodity, or, it may be, to visit new lands and new places by a given route of travel. It collects facts, and places them before the public in an attractive and artistic form. Some one has said that advertising is a mode of education by which the knowledge of consumable goods is increased. It sets forth the peculiar excellence of commodities, and keeps in mind the merits of staple articles. The advertiser is an instructor; he is

not mechanical, but creative. It is said that advertising brings customers to the store, and there its mission stops. Success, then, depends upon the quality and price of the goods and the skill of the salesman.

For a more definite view of advertising problems, a brief examination of the character of the commodities advertised, as well as the tastes of the buyers, is necessary. From an economic point of view the success of advertising is determined by increased consumption, or by better selection. Adequate attention has not been given to the economic aspects of advertising.

A classification of commodities should enable the manufacturer and distributor to develop more effectively their advertising campaign. By a process of elimination a number of commodities are largely excluded from general advertising. This elimination has been suggested by using the classification of commodities ordinarily employed by the economist.[1]

In the first place it is obvious that advertising is not used generally to exploit the merits of raw materials, except in some cases, where they are to be put to special uses. A fair illustration of this exceptional advertising is found in the case of agricultural products. The farmer could not

[1]An excellent treatment of this idea will be found in an article on "The Place of Advertising in Modern Business," by E. Fogg-Meade in the *Journal of Political Economy*, v. IX., 218.

secure an increased price by advertising his wheat, except in rare instances, where his product possesses special merit for seeding. This is true equally of cereals, live stock, cotton, tobacco, and ores. It is true, however, that coal-dealers may advertise a certain kind of coal, but it is rather the advertising of a firm, because the commodity which it offers for sale is generally available to all competitors. Some slight exceptions may be found in the advertising of coal of special quality. In fact, the vast range of raw materials is essentially eliminated from general advertising, except where they possess some special merit.

We now pass to the commodities used in making other goods, such as machinery, and commodities in process of manufacture. The advertisement of these commodities is likewise limited, because their value is determned by fixed and definite standards. The advertising here assumes a special character, and makes its appeal to a special class of consumers. On account of the nature of the commodity, the retailer is not sought. The consumer here is a manufacturer, and he is usually reached by circulars and regular catalogues, combined with a follow-up system.

The advertising possibilities of these commodities are likewise limited, proffered as they are to expert buyers. They can be sold only upon the basis of their recognized value. Moreover, because of the peculiarity of this market, the

efficient advertising media are limited in scope. They are confined almost wholly to trade journals and circulars, and consist mainly of insertions containing a brief statement of the kind of goods. The argument is minimized because well-recognized tests of a peculiar nature usually follow. There are, however, certain classes of goods used in the manufacture of consumable goods, which are advertised somewhat extensively.

We now come to a large class of commodities which is designed particularly for general use, such as wearing apparel, food products, etc. Their value is determined largely by the physical or spiritual enjoyment which they afford us. Special standards and personal tastes, reinforced by utility considerations, are paramount. In this group will be found innumerable kinds of commodities; they are the result of changing vogues, involving every scheme of color and form. Obviously, advertising has here an important rôle to play in fixing the attention of the buyer upon a particular commodity in the midst of a vast variety of similar ones. We have new foods of various kinds, new novelties, new vehicles, new games—in short, new wares of every description. Upon the market will be found more than two hundred varieties of crackers. The difference between these brands is probably not great, and the success of one commodity over that of the one hundred and ninety-nine other varieties is de-

pendent largely upon the adroitness with which the attention of the consumer is brought to it. As styles and tastes change, an ever-increasing variety of goods is offered by the manufacturer, which must be exploited by the advertiser.

It thus appears that the general advertising is confined largely to those commodities which are to be consumed directly by the individual, rather than in the manufacture of other goods. It is the finished product in the form of novelties, notions, wearing apparel, etc., which forms the chief interest of the advertiser. These considerations are important in determining the character of the advertising campaign.

But, before we proceed further, we must briefly consider the buyer in relation to advertising. It is obvious that the methods of advertising will be governed largely by the tastes of the buyer. If we turn to those raw materials which are very little advertised, we find that special methods of distribution have been worked out for them. In the case of wheat, we have a special class of buyers and special agencies for its distribution. The miller or the shipper goes to the Board of Trade. A special market has been created for the cereal trade. The firm only is advertised.

When we come to the purchaser of machinery, we find a special class of buyers, who are not governed in their selection by whims, or personal

tastes, but who are in search for machinery which will give the best results. If a manufacturer desires to buy a steam engine, he uses definite standards to test it. We have thus a set of buyers who possess a knowledge of the machinery which they desire to purchase. Hence advertising forms a very small element in the sale. The firm simply draws attention to the fact that it is manufacturing a given kind of machinery, and relies mainly upon the intelligence of the buyer to determine its merits. In the purchase of these goods the intelligence of the buyer reaches its maximum point, and consequently the work of the advertiser is minimized. A special exception, however, should be made to farm machinery, which is heavily advertised. Competition has doubtless been the cause of this, as well as the lack of technical knowledge on the part of the farmer.

On the other hand, an examination of the goods which are to be directly consumed—as foods, clothing, etc.—will reveal the fact that the tastes of the consumer play an important part. If we accept the assertion that advertising, rightly considered, is a means of educating the consumer, and of developing correct and fixed habits in the selection of goods, the time might come when the individual will not rely to any great extent upon the arguments generally made through advertising, except in so far as they give the information

where specific articles of merit can be purchased.

In the purchase of goods which are directly consumed by the individual, the average intelligence of the consumer is far below that of the buyer of machinery, especially for factory purposes. In the purchase of consumable goods the tests are not so definite, and are largely matters of taste, and are the outgrowth of the personal desires. The growing intelligence of the consumer, however, has a twofold influence: in the first place, it tends to restrict indiscriminate advertising, and, in the second place, to develop its artistic phases. A magazine which will appeal to a highly cultivated class of people will have its pages filled with a different kind of advertising than one whose reading list is composed of a less intelligent class.

In the case of the most intelligent consumers we find that habits, and tastes in selection have been fixed, and the ability to choose highly developed. The wants of the intelligent classes are more varied and intense; but, in addition, the power of selection is more fully developed. For this reason, when they desire to purchase any commodity for their personal use, it will be found that their views are already fixed, but are open to reasonable arguments. Novelty alone plays a less part in the selection, while, on the other hand, quality is sought. The manufacturer recognizes this condition in the business world when he

attempts to make his goods honestly. He knows that advertising cannot hold his trade if his goods are lacking in quality. To this class an effective appeal may be made on the ground of refined tastes, combined with substantial quality. However, novelty with recognized merit, may be a good advertising proposition for the reason that people want something new.

At the other extreme of this great consuming class we find a large body of crude and uneducated consumers. Their tastes are undeveloped and undetermined, and, consequently, their power of selection is weak and ineffective. Their wants and desires have a narrow range. They wear about the same clothes, and eat the same foods, and are usually on the lookout for cheap and shoddy bargains.

To this class an appeal can be made through certain magazines, and papers, but it must be made in a more or less sensational manner. These persons frequent the auction places, and search out cheap counter bargains. They are found in considerable numbers in the slums of our large cities and in outlying country districts. They are usually content with the patent-medicine circular, and kindred advertising literature. In brief, this class often possesses large desires and little power of selection, because of distorted ideas of values and tastes.

By eliminating these two extreme groups of

customers from the field of large advertising, we have now left the middle-class consumers, who are the principal objects of the advertiser's interest. The tastes and power of choice of this class are often dormant and undeveloped. We find here tastes ranging from gaudy display to the more permanently fixed habits of careful and wise selection. Often this power of selection is rapidly developed. We find it expressed in the changing styles of stocks and wares upon the counters of the stores of the larger and smaller cities. Old tastes and habits are being constantly broken up by a process of education and wise selection. It is, therefore, in the midst of these changing conditions that the advertiser finds an opportunity for the exercise of his talent. He finds here a class of consumers whose tastes are capable of development, and, in connection with the manufacturer, he is building up from day to day conservative and substantial habits of selection. The alertness of this class is shown in the advertisements they read and in the interest with which they follow different bargain advertisements of a substantial character. It has shown that advertising is a force working toward social improvement, a means by which the tastes and habits of the masses are revolutionized, and novelty, variety, and harmony are introduced.

As a result of this classification of commodities and consumers, it appears that the advertiser must

play an important part in the whole economy of distribution. The modern system of distribution demands the manufacture and sale of goods in large quantities, and over wide trade areas; this results in strong competition. Advertising is used to increase the sale of these goods by increasing a familiarity with them by exploiting their merits. It stimulates desire and demand, which lie at the basis of our industrial activity. Cheap buying may result, for income determines finally the buying power. The last census returns show that nearly 33 per cent. of all the families of the United States had an average income of less than \$400 per year, or about \$80 per capita; 21 per cent. had an annual income of \$400 to \$600; 15 per cent. had from \$600 to \$900; 10½ per cent. from \$900 to \$1200; 7½ per cent from \$1800 to \$3000.

Advertising fixes new staples by developing a class of consumers who steadily desire new articles, and as rapidly as an article becomes staple the character of the advertising changes. With so many different varieties of the same staple, the trade-mark assumes great importance in the scheme of publicity. By way of summary, it may be said that the advertiser has justified his right to exist from an economic point of view because his work is educational. It tends to develop fixed and permanent habits of selection, which become effective guides to the manufac-

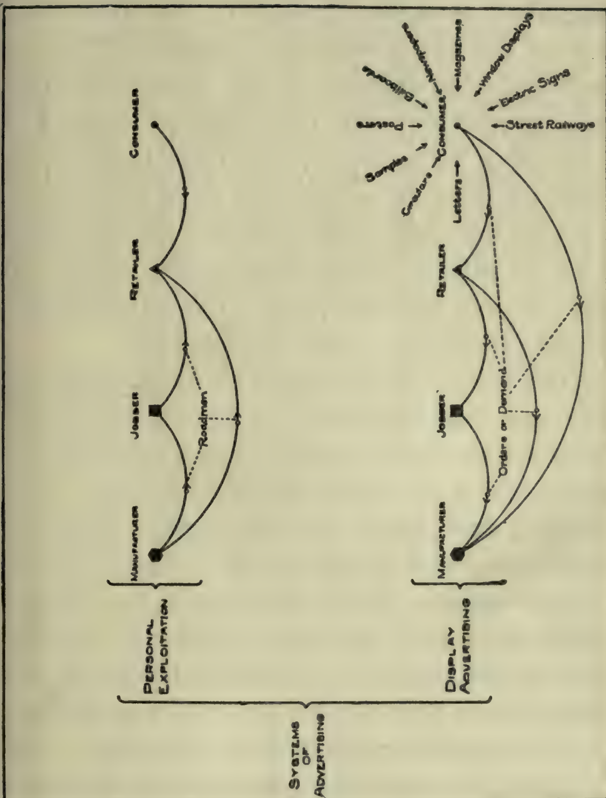
turer in the production of his commodities for the market. In the second place, the consumer is enabled to buy better, and cheaper, by reason of the information and knowledge furnished him through the advertiser; and, in the third place, modern advertising becomes an essential feature of our scheme of distribution.

A great deal has been said in regard to the influence which trusts and combinations exert upon the work of the advertiser. The general contention is that consolidation tends to diminish advertising; doubtless the contention contains some truth. If we take production goods, we find that consolidation tends to diminish advertising, since these are largely controlled by patents, and are manufactured in favored places. It will be also found that combinations are made more generally among those firms manufacturing production goods, and consequently would not affect the field of advertising so decisively as if the combinations controlled consumable commodities. But novelty goods and many articles of consumption are not controlled by trusts and combinations. The conclusion, therefore, is that these combinations do not limit the advertising field to the extent that is generally supposed. It is true that where combinations are possible advertising can be limited. The trusts are large advertisers, not for reasons of competition, but to educate the public, and to increase consumption.

But combinations and consolidations are not so obviously possible in the sale and distribution of consumption goods; and here the great interest of the advertiser is found. In addition to the formation of trusts and combinations, other forces tend to retard advertising, but still do not materially limit the possibilities of publicity in general.

It is doubtful whether the classification of advertising has been made which is accepted by all those familiar with the field. While traveling salesmanship is not considered as advertising in the correct sense, still, it is, however, closely allied to publicity. If, then, we take this broad view of advertising, we find that it very naturally falls into two divisions: first, traveling salesmanship; and, second, display advertising. Under the first can be included that advertising which exploits all wares by word of mouth. It would include particularly the commercial travelers or road-men, who are sent out to push a given line of goods. On the other hand, display advertising includes all those forms which use the printed page, such as bill-boards, circulars, magazines, and newspapers. The last division may be still further subdivided into general and special advertising, the latter including in the main local retail publicity, the best instance of which is department-store advertising.

The following diagram will convey a more


Systems of Advertising
Personal Exploitation
Manufacturer
Jobber
Retailer
Consumer
Roadmen
Display Advertising
Manufacturer
Jobber
Retailer
Consumer
Orders or Demand
Letters
Circulars
Samples
Posters
Billboards
Newspapers
Magazines
Window Displays
Electric Signs
Street Railways

vivid notion of the relation of these two systems than can be given in any description: (p. 309.)

These two systems of pushing sales are rarely employed separately except by the mail-order houses, but are more often combined. The second method of exploitation was through the commercial traveler. The main purpose sought was to bring a particular ware to the attention of a local merchant or retailer and leave him to supplement the work of the manufacturer or wholesaler by calling the attention of the customer to the merits of the commodity. The appeal is made to the retailer and not to the consumer.

The danger of this system obviously lies in the fact that the retailer too often over-stocks with undesirable goods before a demand is created for them. This has often proved disastrous to the retailer and, finally, to the manufacturer and wholesaler; it does not provide a steady demand for the output. The general result is a demand artifically created, because it is easier for a skilled commercial traveler to persuade the local merchant to buy than it is for the retailer to persuade a hundred consumers to take the goods. Furthermore, it places the manufacturer, and often the wholesaler, at the mercy of traveling salesmen, who develop an acquaintance among the retailers which is often influential. This is frequently employed to extort important concessions

from the wholesaler, and frequently he in turn demands concessions from the manufacturer.

As a consequence of the unsatisfactory result which attended the system of direct exploitation by the traveling salesman, display advertising has been rapidly developed. Its rapid growth is largely due to the efforts of the manufacturer to free himself as far as possible from the control of the wholesaler and retailer by making his appeal directly to the consumer; he creates a logical condition. If the manufacturer produces what the people want, he should control the situation and should not be at the mercy of mere handlers of merchandise. His investments compel him to take this view. The theory of display advertising is radically different from that of traveling salesmanship; the central idea is the direct appeal to the consumer. The advertiser surrounds a consumer with every possible suggestion of the merits of a particular ware; every form of printed matter is put before him, setting forth the merits and qualities of given commodities. On the bill-boards, in the daily papers, in the magazines, in the street cars, and in his mail in the form of circulars and letters, and, in fact, on every side the consumer meets suggestions and arguments for some particular commodity. As a result there is built up a desire to purchase it. The effects of this class of advertising are cumulative.

The same influences are at work throughout the community, and a desire for this commodity has been aroused in a hundred consumers. They may not all be trading at the same store, but each goes to his particular place of trade and asks for this commodity. The retailer may not have it, and may not even have had his attention called to it until his customers began to make inquiries for the ware, but when this demand from the consumer becomes appreciably felt, the retailer is bound to send in an order to the manufacturer or wholesaler.

The merits of publicity advertising, as compared with the other system, lie in the fact that direct appeal to the consumer has created a demand for the commodity, which cumulates as we pass from the consumer to the merchant, wholesaler, and manufacturer. This system permits the local merchant to make his orders in response to a demand, while, in the case of the other system, his orders are made in the hope of demand.

We will first take up the examination of display advertising. We must keep in mind the fact that this system has in view a direct appeal to the general public. The idea is to impress upon the mind of the customer the qualities and virtues of specific commodities. Display advertising falls into two classes based upon the character of the appeal to the consumer. Into one class fall those advertising efforts which are

general in their character and do not have in mind a direct personal appeal so much as the creation of general impressions. This is sometimes called *general publicity.* It is designed to call general attention to a particular brand or ware, but not to advertise in a specific way. No place of purchase is designated, but the customer is permitted to go to his regular place of business. By way of illustration, we may take the outdoor advertisement of Pear's soap, or Sapolio's stories of Spotless Town. Cigars are often advertised in this way. The media ordinarily used for general publicity are the bill-boards, street cars, newspapers, magazines of general circulation, and other media with which the public would come into contact in large numbers.

Advertising should not be confined alone to competitive lines, but should be employed to create new wants and to exploit the merits of new articles. Necessities are subject to strong competition, and while they may vary from time to time, they are easily distinguished from luxuries. The necessities of our modern life are many; and, because of the universally similar conditions of living, are in universal demand. For this reason, articles of apparel, food, shelter, household, and utility include a wide range of necessities, and are readily adapted to the principle of general publicity.

A second class of display advertising may be

designated as direct or specific advertising, where the merchant or manufacturer makes a special argument in exploiting his goods. This is sometimes known as "educational," or "reason why" advertising. To the advertisement is usually attached a price and a place where the article can be secured. Direct advertising is carried on as a rule by the local merchants, retail stores, and the mail-order houses. The object is to direct the customer in a specific way. A good illustration is found in "Monday sales" of large department stores, or the "leaders" of local retailers.

These two systems are generally combined in the campaign of publicity, the general advertising being used more often by the wholesaler or manufacturer, and the specific advertising by the retailers and mail-order houses. The reason for this division of labor is obvious. The local dealer will understand more particularly the wants of his trade and the method of appeal than the wholesaler or manufacturer. An illustration of the combination of general and direct advertising is found in the manner of placing proprietary medicines upon the market. Often the medicine will be advertised in a general way, combined with the specific statement that such medicines can be procured at the drug store. Mellin's food is often advertised in a general way, and then supplemented by a more specific argument as to quality, price, and place of purchase. The two systems

are generally separated, but, in fact, must be considered together as forming an organic and complete scheme of publicity. It should, however, be observed that the manufacturer and wholesaler are both using the argumentative form of advertising more extensively. Advertising has even become more than keeping a name before the public; it is salesmanship upon paper.

The character of display advertising may be further simplified by referring to the different media which are employed in placing the goods before the public. These media may be classified in different ways. One classification is as follows: In the first group is placed the periodical press which forms the most effective and important means of advertising. These media go directly into the home and upon the reading tables, and are consulted constantly. As a result, commodities of general utility are likely to be brought to the attention of the reader in a more effective manner through these media than where they are advertised in special ways. Of the periodical literature, probably the most widely used is the daily paper, because it is published in the great trade centers and is generally consulted for local trade purposes. Wilson found that 32.1 per cent. of the space of 147 leading dailies of the United States was devoted to advertising in the following proportions: 54 per cent. want advertisements, 13.4 per cent. retail, 3.9 per cent.

medical, 2 per cent. political and legal, 6 per cent. miscellaneous, and 1.4 per cent. personal advertisements.

The value of the daily paper may be illustrated by a competition for advertising space which recently took place in Philadelphia between two great department stores. It is said that Wanamaker paid the *Record* \$87,000 for a full page each day for one year, but the price of \$105,000 for a renewal contract was asked. Mr. Wanamaker refused, and his leading competitors, Little Brothers, accepted the proposition. The value of the daily newspaper may be further illustrated by some statistics relating to the advertising of Mr. Wanamaker. It is stated that he used a page per day in the leading dailies of Philadelphia at the following prices for a given year: the *Press,* \$60,000; the *Ledger,* \$60,000; *North American,* \$75,000; the *Times,* \$50,000; and the *Evening Telegraph,* \$50,000—a total expenditure of about \$1,000 per day. These figures convey some idea of the enormous value of the space of the daily newspaper for advertising purposes. It is based upon extensive circulation, and particularly upon the fact that it goes daily into the hands of the customer.

Another important group of periodical literature is the magazine of general circulation. These magazines of general interest and circulation carry a very considerable amount of adver-

tising. This space has increased very rapidly in quantity and also in price. General magazine advertising began about twenty-five years ago. The more important magazines carry about one hundred and fifty pages of advertising. Another group of periodical literature, possibly of less advertising importance, is the weekly paper. The weekly newspaper does not have the circulation that it formerly enjoyed, with the exception of those devoted to special interests and fields, and also some which have virtually taken the position of a magazine of general circulation, such as the *Outlook, Harper's Weekly, Collier's,* and *Saturday Evening Post.* The rural mail delivery is increasing the value of the weekly.

In addition, we have the trade journal, a periodical magazine which is devoted to special lines. These are of great variety and follow the law of specialization in business. Naturally, they afford a splendid means of reaching the buyers of special goods. Their appeal is very direct and specific, because it is assumed that the reader has a special and personal interest in the field which the magazine represents and cultivates. They are published for the trade, and go to a select class of readers, usually to the retailers and buyers.

Finally, we have those periodicals cultivating a special field and offering, for that reason, a splendid medium. For instance, *System* appeals to the business man; *Outing* and *Country Life*

appeal to the lovers of nature and outdoor life. The organs of religion—especially of a given Church—of political parties, or of a social set, fall into this group, cultivating a class of readers of special tastes. The periodical press leads all other media in the amount and variety of advertising carried.

A second class of media may be designated as occasional literature. These are sent out, as a rule, by firms to exploit their own commodities. They usually consist of circulars in a broad sense. The most familiar are letters, almanacs, calendars, circulars, catalogues, booklets, etc. They are usually mailed to the consumer. They form a very important means of interesting the public, and are employed for a variety of purposes, such as calling attention to the change of styles for the seasonal trade. They are often used to develop new territory or to work old territory more thoroughly. They are employed by manufacturers to call the attention of the jobbers to special lines of goods. Many firms issue organ publications to exploit their goods at reduced postage rates.

But probably the most important use to which circulars and catalogues are put is found in the mail-order business. The mail order is based almost exclusively upon circular advertising, and while the mail-order firms employ general publicity, they rely almost exclusively upon circulari-

zation in developing and holding the trade. Of course, this class of media is used exclusively in the "follow-up" system. Almost every business makes use of the circular to some extent. Circularization is now considered indispensable, and is put to wide use in the general campaign of publicity.

When the "call-up" and "follow-up" systems are used, the advertising office has many varieties of letters suitable for particular cases. A careful record is kept of the letters sent to each party. The news columns of the different trade journals are consulted and inquiries started to ascertain the needs of the firms expanding their business. The clipping bureau is extensively used in collecting information, and a manufacturer receives, as a rule, advance sheets from his clipping bureau which give him specific information concerning firms desiring his output. The first inquiry is followed up with three or four letters.

A third and final class of media may be designated as outdoor advertising. This phase of advertising is the outgrowth of a desire to utilize space for display purposes where people congregate or pass frequently in large numbers. The most important of these are the signboards of stores, the posters upon the sides of buildings and along streets, the printed signs that stand at the entrances of shops and offices, the movable posters and signs which are sent out by manufacturers to

be placed in conspicuous places in stores, the electric sign, and, finally, the street-car space. Outdoor advertising has a certain value which is determined by the character and density of the population. It is a general plan for merchants to follow display advertising out into the rural districts, along the highways, and the larger wholesale stores of the cities even follow the railroads out for considerable distances, where people may read as they ride. This form of advertising is handled, as a rule, by special advertising agencies, such as the Gunning system, who buy up and control space in many communities. The billboard advertisers are very strongly organized. While street-car advertising is only about fifteen years old, still, thousands of cars carry advertising of great value.

This classification includes the principal media, and, while all have not been mentioned specifically, they would fall in one of these classes. The mere enumeration of these media conveys some impression of the vast field of advertising. When we consider that, of the periodical press alone, in the United States we have about 20,000 magazines and papers, having a circulation of many millions, we can form some conception of the opportunity of the advertiser. At the same time, he is confronted with great difficulties in placing his appropriations for advertising. Who

can answer the question, What is the best form of advertising for any particular commodity?

We must now turn to the consideration of the more technical side of advertising. We have here to note some of the considerations relative to the construction of the advertisement itself and the development of the advertising campaign. We shall assume that the advertiser has placed his proposition in the hands of a regular advertising agency, or has at the head of his advertising department a trained and experienced man to develop his campaign of publicity.

The advertising manager has before him a specific proposition which he must take up and develop as a continuous policy. The first step in the development of an advertising campaign is to become fully acquainted with the character of the ware to be advertised. A careful study of the commodity or service, and the use to which it is to be put, is followed by an examination of the class of customers who are likely to be interested in it. After these two very vital points in the campaign have been examined, the territory which is to be advertised must be determined upon, and, finally, whether extensive or intensive advertising is desirable. With these matters fully determined, a careful study of the different media must be made. This relates to the character of the circulation and to the class of readers. For final determination, the controlling element in the

selection of the media is the reader. Who reads the medium? Is it read by men, women, and children? Does it go into the home or the office? Is it of general circulation or is it a trade medium? People of refined tastes and judgment in selection read a different class of literature than those of indifferent tastes. The selection of a medium is important. A high-class magazine lends tone to the advertisement, and the confidence of the reader in the medium is often of more value than mere circulation; tone is essential.

After these facts have been determined, the advertising manager develops his argument and his appeal. The argument is determined by the considerations noted above. In order to be effective it must be truthful, distinctive, and to the point. These elements are growing more valuable each year in high-class advertising. Another factor of growing importance is the character of the media. The owner of publications will not accept any sort of advertising. It is difficult for advertisers of questionable articles to buy space in high-class media, and in this way the advertisers of legitimate articles are protected. Confidence in the publishers invites confidence in the merits of the goods advertised.

After all these matters have been settled, the advertiser develops his campaign and carefully works out all its details. He looks after the composition of the advertisement, the selection of

illustrations, the literary form, the position on the page. The construction of an advertisement involves the selection of type, borders, cuts, literary style, head-lines, body, argument, and position. He determines whether new advertising is to follow. In fact, all matters are left to his judgment. The nature of the campaign is virtually determined by the value of the commodity which is placed upon the market and the amount of money which is to be expended in publicity. The cost of the advertising campaign will, of course, be determined by the value of the commodity and margin of profit. The value of advertising is difficult to measure, because it is service, and material standards will not suffice.

No better illustration of the influence of environment upon advertising is afforded than by a comparison of Massachusetts with the Pacific Coast. The three States of California, Washington, and Oregon are forty times the size of the State of Massachusetts, and yet there are 248,600 more people in Massachusetts than in all of the Pacific Coast States. The Massachusetts territory is compact, and we find here a varied market in a small and populous area, and consequently advertising can be made to yield larger results. For this reason, the advertiser will seek populous and compact areas rather than the extended ones of the Western States in which to launch his advertising campaign; especially is this true of

outdoor publicity. It can, however, be urged with force that the Western field, or less populous areas, may at times yield better returns in proportion to the money put into advertising, for the reason that the competition of advertisers is less severe as compared with the populous areas.

In order to make the advertising campaign effective, it must be a continuous and permanent policy; sporadic and intermittent advertising carries little weight. It is the constant appeal which leaves its impression and secures the trade. The specific advantages of publicity, from a business man's point of view, are the enlargement of his business field, maintenance and prices, an assured trade, the simplification of business, and an independence of the distributor. The business man cannot afford to wait for trade. He must induce buyers to come, or else failure or half-hearted success lies before him; he must send forth his appeal through the channels of advertising.

A most important advantage accrues to the manufacturer who establishes his trade-mark. It is by the use of this symbol that he gains the confidence of the public and secures a large degree of independence of the wholesaler and retailer. Through the medium of advertising, the trade-mark has attained a position of great importance in distribution. The trade-mark distinguishes the article of one firm from those articles of a

similar kind and nature. It identifies the commodity with the established reputation of a firm. The manager has succeeded in identifying his wares with the trade-mark after time and expense. It has no existence apart from the article. All lines of business use this protection extensively, and both the manufacturer and the wholesaler have discovered its importance.

When a firm is fully established, the trade-mark becomes a great force in advertising. It is an important element in the formation of the argument, it is a guarantee of quality, and enables the consumer to make sure of his purchases. The same remarks apply equally to brands. The brand applies to a given article, is a convenient method of establishing its merits, and affords a ready way of distinguishing it from articles of a similar kind. For this reason, it has likewise great advertising value. In competition the significant thing is to bring the article above the level of mediocrity, for excellence has naturally great advertising value. For this reason, the trade-mark or brand is effectively employed. Illustrations of its use are innumerable, for in almost every line of business it is found. It is the index to the article, and stands in the minds of the customer for a definite value. Among the well-known and largely advertised trade-marks are Pear's soap, Towne's gloves, Kaiser's cravats,

Hannan shoes, and Dunlap hats. The list could be extended indefinitely.

One who advertises in a general way an article sold at retail finds that it is more effective to be able to designate it by a specific name than to refer to it in general terms. It is for this reason that the trade-mark and brand become of tremendous value in appealing to the customer. These articles are then distributed through the general channels of trade. The result is to make the trade-mark goods the principal stock of the distributor. Generally, staple articles are sold under trade-marks.

The trade-mark has special value because of the fact that it can be registered, which gives the owner protection in its use. It is, therefore, essential to select a good trade-mark and have it properly registered. The registration of the trade-mark is made with the Patent Office, and the certificate of registration is recognized by the courts as *prima facie* evidence of the ownership of the mark. It is because of this legal protection, as well as of the great service to the owner by way of identification and the protection from imposition upon the customer, that the trade-mark possesses such great value in distribution; for these reasons its importance can scarcely be overestimated.

Systems are often employed to determine the results of the advertising campaign. It is often

difficult to determine which media are best adapted for publicity. Some advertisers attempt to keep a record of the results of advertising in the different media. This is technically known as "keying," and various methods are employed to determine this. One of the more familiar ones is to give different addresses in different magazines. In some instances trade numbers are employed; in other cases, department letters and numbers are used. One of the more recent methods is the coupon system; by this method space is left in the advertisement to be cut out by the customer and mailed to the advertiser.

All advertisers, however, do not attempt to determine the value of advertising in any definite manner, but count upon a certain amount of money to be devoted to publicity and look to final results in sales. This is true especially of general publicity. It is assumed that the bulk of purchases at retail stores is the result of information and suggestions from advertising, and that any scheme or tabulation cannot be trusted adequately to furnish a basis of a judgment as to the value of a given medium. Mail-order advertising, however, can be successfully "keyed."

The amount of money to be put into the advertising campaign will vary according to the circumstances. It is said that proprietary medicine firms often put as high as two-thirds of the receipts into advertising. This is due probably to

the fact that the cost of the article is relatively small, and the margin of profit large, and that publicity is virtually the principal invesment. The amount put into publicity will depend upon the article and the average sales. Obviously, there is a point where increased expenses for advertising would not bring proportionate returns. The appropriation for advertising is largely dependent upon the margin of profit; this in turn affects the form of the campaign. Articles of small profit usually have strong competition, so that it is necessary to begin in a small way, make the advertisement pay for itself, and gradually increase the appropriation in proportion to sales.

In order to give some indication of the cost of advertising space, we insert here a list of the leading magazines, together with the publishers' rates and circulation. Obviously these statistics are constantly changing, but they will afford some idea of the value placed by the publisher and advertiser upon space for advertising purposes. The generally recognized rule for determining the rates for advertising in the standard media of general circulation is one dollar per page per thousand circulation, and any change of rates is usually based upon this standard of value. There will, however, appear discrepancies in the application of this general rule, due to the fact that

some magazines are of a recognizedly higher class than the average.

ADVERTISING RATES OF THE LEADING PUBLICATIONS

PUBLISHERS LIST RATE

PUBLICATION	PER PAGE PER ISSUE	CIRCULATION
Cosmopolitan - - -	$ 350.00	450,000
Everybody's Magazine -	500.00	650,000
American Illustrated Magazine	200.00	227,000
McClure's - - - -	384.00	400,000
Munsey - - - -	500.00	800,000
Century - - - -	250.00	150,000
Pearson - - - -	200.00	225,000
Review of Reviews - -	200.00	180,000
Scribner's - - - -	250.00	150,000
Success - - - -	1,000.00	300,000
Ladies' Home Journal -	4,000,00	1,000,000

Before closing this discussion, we desire to call attention to some of the features of the mail-order business in its relation to advertising. This business is based entirely upon advertising, since it is through general publicity and the circular that the mail-order house receives its patronage. In the first place, there must be secured a list of the possible purchasers to whom the circulars and catalogues of the firm are mailed. The catalogue takes the place of the traveling and counter-salesman. It goes into the home, and cultivates and holds the customer by the carefulness with which the orders are filled and the

giving of right values. This kind of advertising is different from general advertising in that it must be very specific and correct as to description of article and price. Any error or dishonesty in filling the order would naturally result in disaster to the business. This business has grown to enormous proportions, because it is usually carried on with the rural communities and small cities. The advertising is intended to displace the traveling salesman. The success of this system is shown in the rapid rise of the firms of Sears, Roebuck and Company, and Montgomery, Ward and Company, of Chicago, which have built up in a few years an annual business of many millions of dollars.

It is natural that the enormous amount of money put into publicity should develop highly trained and specialized talent devoted to the development of advertising campaigns. The purpose of this discussion, as well as the limitations naturally imposed upon it, prevents any extended account of the different phases of specialized effort found engaged in the present-day advertising. We can, therefore, go no further than to mention some of the professions that have come into existence during the last few years as a result of advertising efforts.

At least three well-marked professions have been developed as a result of modern publicity. These are the advertising expert, advertising

manager, and the advertising solicitor. The first is the adviser of clients; it is his business to sell professional service. His compensation comes from commissions from the publisher. There is no money saved by the advertiser in dealing directly with the publisher. The latter allows the agent a commission in order to encourage him in securing business, for the reason that professional handling usually increases the advertising appropriation, and also because the business comes in bunches and on time. It is customary to-day for a large number of advertisers to place their business with advertising agencies. Their function is to map out and manage the campaign of publicity for the advertiser. Some of these, however, have grown to large proportions and their work reaches out to every market. The services of the advertising expert are in greater demand to-day than formerly, because of the growing recognition of the scientific character of modern advertising.

In addition to this class of advertising experts, every important manufacturer and distributor has attached to the business an advertising manager. In some instances this manager maps out the campaign of publicity for the business he represents independently, or in connection with advertising experts. Some very large concerns have a fully equipped advertising department, with artists and printing establishments, and are in a position to

prepare complete copy. In such cases, the agency acts usually as the professional adviser, and sometimes handles the business at a lower rate than the customary one. In this instance the advertising manager keeps a record of the advertising space with the agency and sees that it is properly executed.

Finally, we have the advertising solicitor. It is the function of the solicitor to go out into the trade and solicit advertising. He represents either a publisher or an advertising agency. In addition to soliciting, he gives advice as to the proper methods of advertising the commodity and in the selection of media. This is, however, incidental, for his principal function is to sell advertising space. Much creative work is expected of the solicitor. He is primarily the traveling agent of the publisher, or the advertising agency.

This outline of advertising is intended primarily to gather into a convenient form the most approved ideas on advertising, and is not intended to be in any way exhaustive, nor to lay down in any dogmatic way advertising principles. A survey of the field will readily indicate the impossibility of reducing advertising to a set of rules which would be accepted by all advertisers. While a great deal has been done to systematize the data and facts in regard to advertising, it cannot, however, be termed a science. All that

can be said is that it is better understood to-day than it was a few years ago. The expert is in a position to indicate probable results by reason of his comprehensive knowledge of facts regarding advertising media and the conditions of trade; as a result, his methods are more effective. It has been our purpose to indicate the leading considerations that must be reckoned with by those who use advertising as a means of developing their business. While little is published upon the subject of advertising which would receive general acceptance, still, varied discussions exist which have been freely consulted in the preparation of these pages.

Advertising may be summarized briefly as the power to attract the attention of the consumer, to stimulate an interest in the article advertised, to create a desire to possess and enjoy it, and, finally, to lead to the resolution to purchase it. These steps may not come to the customer upon the first notice of the advertisement, but by frequently coming into contact with it the final result is generally attained.

XIV

CREDITS AND COLLECTIONS

Recently great attention has been given to the development of a safe policy of granting credits and of making collections. In every highly organized industrial society, credits have always been extended and collections made, but in very recent years competition has forced a more scientific interest in the subject. In the earlier stages of our industrial movement, business was done on a wider margin of profit, and economy and carefulness were not so important as increased production. The willingness to buy was taken as an index to the ability to pay. Because selling was done in large quantities on a wide margin, the matter of credit was unimportant. These conditions made business successful as a rule, although collections were often difficult and losses were frequent. In short, a few years ago a careful control of credit was minor and incidental, and collections remiss.

During the last few years all this has changed. Competition has narrowed the margin of profit until the time is at hand, in most lines of business, when economy must be most carefully practised. This consists, not only in reducing the expenses of

business, but also in preventing losses which formerly resulted from the loose system of credits in vogue. A decreasing margin of profit compels a more definite understanding of credit conditions. Under these circumstances the long credit of former years must be shortened; money must be turned over. As is the case with advertising, there are no infallible rules governing the granting of credit, but a more definite knowledge and practise are growing up.

The improvement of recent years has been mainly along the lines of method and organization. Firms have been compelled to install credit departments; formerly these duties were undertaken largely by the general manager. Mercantile agencies have come into existence, pushing out into every confine of business activity, and a more searching analysis of buying and paying capacity is the result. The importance of this new movement is forcibly indicated by the annual estimated saving of $25,000,000 in normal times. But the indirect influence is also very great. It builds up business stability and prevents abnormal buying; it discourages over-stocking. The very fact that it is estimated that ninety per cent. of our commercial transactions are done on credit makes evident the value of a careful knowledge of credits.

It is not our purpose to enter into an extended discussion of the economic aspects of credit.

Credit begins when the owner of the commodity is willing to part with it until it is received back, or until its equivalent value is returned. Under the old economic order there was a traffic in goods. Under the new order trading is done on a capital basis with convertible values. There are, then, two forms of credit—the loan and the credit proper. As business expands and wants multiply, the need of capital calls into use surplus funds in the form of loans. With the exchange of commodities it is customary to pay in cash at or near the time of delivery. This calls into activity the other side of credit, which consists in carrying the commodity, or its value, upon the books of the selling firm in the form of an account. The wide use of credit in any form in business is made possible by the development of an accepted money standard of value. This makes possible contracts involving future payment.

Credit, in a popular sense, simply means the ability to purchase a commodity upon the promise to pay for that commodity at a future time. It is determined by the seller's confidence in the honesty of the purchaser; but, in a commercial sense, credit is something rather different. In the commercial sense, it is something more than confidence, and rests upon a more tangible foundation. It must be based upon accurate information concerning the reasons, assets, and ability of the buyer to meet his obligations. Com-

mercial credit is based upon ascertainable resources, which can be converted, if necessary, into equivalent values; still, just what is, in any given case, a safe prospective credit cannot be rigidly fixed. The successful business man must always take this into consideration; if he does not, there are many lines in which he cannot continue in business. The cash system is not sufficiently universal in most lines to make business operations successful.

Having before us the more important considerations in regard to the business man's view of credit, we will pass to an examination of its elements. Credit rests primarily upon two sets of values, which may be designated as tangible and intangible values. Naturally, the more important of these is the tangible value, which goes back to visible, calculable assets and resources. From the point of view of the firm granting credit, these must be convertible; they must be measurable by other values. They must have a value upon the market. The possession of marketable property is the first essential of credit.

The whole structure of commerce rests upon the exchange of articles at normal values. The debtor must possess marketable commodities. He must be able to distinguish between capital and credit. What may appear to be capital may prove to be credit secured from other sources, or, in other words, debts. It is not always easy to

draw the line between property and actual debts. From a business man's point of view, capital is equivalent to money values; it is a convertible asset. The current business phrase for this kind of credit is that "credit is as good as money." When credit is extended beyond this point, a large element of chance enters into the transaction.

When a grocer buys of a wholesale merchant on credit, he pledges his unencumbered or unpledged property for the payment. The manufacturer pledges his unfinished goods to the banker for ready cash; credit is extended upon the business as a going concern. It will thus be seen that credit calls for a special determination of resources and liabilities. It makes capital more effective, and keeps it in productive channels.

The whole problem of a tangible value is summed up in the question, *Can* the debtor pay? and not *Will* he pay? Of course, the latter element enters, but his ability to pay must rest upon his marketable property. A good credit risk, therefore, goes back to tangible values. In credit parlance, a good risk is an advance of credit to a reasonable percentage of the value of the marketable goods in process of conversion into money. Tangible assets in the way of property should be distinguished from an extended line of credit. Actual resources should be taken conservatively, for the reason that they may not be readily changed into cash.

In passing upon capital as the basis of credit, the judgment must go back to the relation of the volume of sales to the capital invested. In other words, the merchant must sell his goods. Something more than salability is required. The rapidity of the sale, or conversion of capital must be known or approximately ascertained. In the majority of instances this is a controlling element in extending credit. We can illustrate this principle by the dry-goods business. The merchant may have a well-stocked store, but the sales must move with a certain rapidity before he can do a profitable business. It is estimated that stock must be turned over in the dry-goods business at least twice each year in order to make the business profitable. The turnover is, then, an all-important feature of mercantile lines.

In determining the nature of the turnover, two elements are involved: first, its magnitude, and, second, the length of time required. The merchant is struggling to shorten this period and puts it in such concrete terms as quick sales and small profits. In order to accomplish his purpose, he adopts usually two methods to shorten the period of the turnover: first, by adopting more economical processes, and, second, by increasing the rapidity of the sales. Obviously, the rate of the turnover is more important when associated with the volume of the business. It is the effort to increase the volume of business that leads the

merchant to resort to credit either in the form of borrowed capital or in the form of time credit. The ability to make an analysis of these facts in their various relationships makes a good credit man.

In order to determine a line of credit upon a going business, the credit man must know whether the debtor is doing a profitable business. It is not always easy to determine this. The rate of the turnover and the volume of the business cannot always be definitely ascertained. One of the well-recognized methods of ascertaining these facts is to require a statement from the merchant. This is merely a starting-point, and is often considered by the credit manager of doubtful value; still, the commercial world and mercantile agencies require it. Other means are also used, such as reports of salesmen, and other information.

While the tangible asset must necessarily be the largest consideration in determining a line of credit, still, the intangible assets are of the utmost importance. These are always present, and credit judgments in respect to them are the most difficult. It is upon this point that the credit manager must be ever alert. He must be able to place a proper value upon them, and while they are often difficult to ascertain, nevertheless they have great commercial value. It is a recognition of the fact that a merchant's credit does not alone consist in convertible money values, but other

elements of the utmost importance must be considered. A value can be placed upon data which can be collected and measured by recognized standards in business practise.

We may now turn to a consideration of the elements which go to make up the intangible assets or values. Many of the more important ones are patents, trade-marks, franchises, copyrights, and similar legal rights. These have great value, for they often protect the firm from excessive competition; it is readily admitted that all do not. It is the business of the credit manager to assign to them a value as an element in granting credit. To possess these assets is not sufficient to secure credit, but when brought into relationship with a going business they are often of great value.

Another intangible element goes back to the manager of the business. The most essential element is the capacity of the man at the head of the business. Business efficiency, coupled with honesty, is evidently a very important consideration in extending credit, but it is often difficult to place a value upon capacity, for it involves careful buying, care in management of stock, treatment of customers, and the methods of giving credit and making collections. In short, business conservatism is compatible with progress and thrift, and relates to the reputation for fair dealing and standing in the community; this goes

back to the payment of debts and whether fraud is practised or not. It must be ascertained whether the business is on a sound or speculative basis. It is estimated that fifty-three per cent. of failures are due to lack of capital, ignorance, and inexperience. Character and ability have no value alone in the business world; but they become exceedingly valuable when brought into connection with capital.

The above factors relate to what is usually termed business confidence. In the commercial sense, they must have a business foundation. All of these elements combine to form the element usually designated as "good will" in business. This is everywhere recognized as having commercial value, and the law gives it a recognition of considerable importance. The established reputation of a firm has commercial value, and the credit man must consider these elements in extending credit.

Another intangible asset of great importance is the nature of competition. Especially must this be carefully considered in granting credit to local merchants. A number of elements enter into the determination of this fact. Is the store inviting, and well kept? Are the clerks courteous? Are the goods well displayed? Is the advertising effective? Do the prices permit a profit? These are recognized as essential facts in retailing. Competition is always strong, and trade goes

where it is invited, and remains where it is well treated. It is recognized, in retailing, that a business is worth what the competitor permits it to be worth. Therefore it is quite obvious that the conditions under which the local merchant conducts his business are vital in determining the amount of credit to be extended to him.

Having now before us the elements which constitute credit, we may turn to the organization of the various agencies which have come into existence for the purpose of collecting and systematizing credit information. These agencies are confined largely to mercantile lines. Of course, every large firm engaged in manufacturing and distribution has its credit department, but there are several classes of mercantile agencies engaged in collecting credit information.

To one class belongs the general agency covering every mercantile house which gives and receives credit, the most conspicuous examples of which are the Dun and Bradstreet agencies. These general agencies in some cases also operate in a limited territory. To the second class belong the special agencies covering special kinds of mercantile firms. To the third class belongs the credit clearing-house. This central institution collects the data and renders a statement to the firm of the credit standing of customers. To the fourth class belong those mercantile agencies of a local character. They are usually designated

as local credit associations, and are organized to cover the local field for the retail merchant. They usually take up the work where the general or special mercantile agency ceases, and are frequently organized co-operatively by the local merchant. The fifth class includes the credit department of the various houses which pass upon the credits which are to be extended upon specific sales. It is quite obvious that the whole problem of credits is so extensive and complicated that no one of these agencies can gather and present conclusive evidence of the financial standing of all firms. The special mercantile agency and credit department of the different firms are organized to supplement the work of the general agency. They shape their work in their special line with reference to the scope of the general agency.

The mercantile agency is a bureau of information with respect to the field it covers. It had its origin in the panic of 1837, and since that time has grown rapidly in numbers, influence, and helpfulness, as a result of increased competition and the falling margin of profit. They originated in the exchange of information respecting debtors among the business men of New York City. Small fees were charged for this service, rating books were published, and branch offices were established for the collection of information.

Taking the general mercantile agency as a type, we may now pass to an examination of its

organization and methods. The purpose of the agency determines its organization. Its function is to collect and systematize data in regard to the financial standing of all persons doing a mercantile business. In order to do this, an organization must be kept in search of this information, which must be edited and given out to subscribers.

Several general agencies are scattered over the country, but the principal ones are Dun and Bradstreet, and the United States Mercantile Agency. These list all kinds of firms, from the modest retailer to the great corporation. The classification of the business follows two lines. The first division is made upon the basis of wholesaling, retailing, and exporting. The second division is according to territory. A central office is usually found in New York City, with many branch offices in the leading cities of the world; one agency has nearly two hundred offices in the United States alone. The degree to which a territory is covered will be determined by its trade importance. In some instances a local office is opened up with its special reporters, while in other instances only occasional reporters are employed.

Reporting centers are established at the important trade markets. These branch offices have an assigned territory to cover, which is done in two ways. In connection with these offices are stationed special reporters, who are sent out into

the territory to gather specific information in regard to the credit of the different firms; these are specially trained men, and often are accountants. They are expert in searching out the truth from conflicting statements. The work of the special reporter is supplementary to that of the resident reporter in the smaller places. At every court house, and often in other places, is stationed a representative who keeps the office informed concerning failures and business changes affecting financial standing.

This extensive organization means the employment of thousands of reporters gathering data in regard to the financial standing of the firms covered by the agency. In the large cities the work is specialized. One division of reporters is placed in charge of the wholesale business; another is placed in charge of the territory outside of the business center. Often each district has sub-offices in lesser cities, and may be further divided into smaller reporting districts. In every town and city, attorneys are employed, and in this way every hamlet and important firm asking credit is covered.

It will thus be seen that the country is divided into districts in charge of superintendents with offices located in an important city. For instance, Wisconsin forms one district with the main office in Milwaukee. In the larger cities of the district are agents who devote their entire time to the

interests of the agency, but in the smaller towns and villages the work is done by men engaged in other business; this person is usually a lawyer or a banker. In addition to these, representatives travel through the district at irregular intervals to examine into the work of the agents. In large cities two or three men are stationed to carry on the inquiries necessary to the business. In Minneapolis three such men are employed.

We may now turn to an examination of the sources from which the reporters secure their information. For this purpose it is usual to divide the business into different classes. Usually two classes are recognized: first, the manufacturers, jobbers, and wholesalers; and, second, the retailers. The method of securing data for the first class is quite uniform, while for the second class uniform methods are not always feasible.

In order to form a correct judgment as to the financial standing of a business firm, it is necessary to secure data from different sources, so that comparisons may be made before a final judgment is reached. One course very generally employed by mercantile agencies is to require a financial statement from the firm itself. In addition, the reporting agency requests a monthly statement of outstanding accounts. By tabulating this, the total indebtedness is obtained, and by comparing it with the assets, a fair idea of the financial standing of the merchant can be obtained. An-

other source of information is the reports of local correspondents and traveling reporters.

The task of classifying the information secured at the branch and central offices is scarcely less difficult than that of collecting it. Credit information must be carefully systematized and made available for use. Delays cannot be tolerated, because it often means the loss of an order, or it may result in extending credit which may prove a long risk. The card system of record has greatly facilitated the classification of credit information, and has rendered it much more available.

The general agency makes its information known in three different ways: first, through the quarterly and annual directory; second, through daily sheets and reports; and, third, through special reports. The directory contains the names of all the firms doing any important business in the United States, arranged by States and cities with an assigned rating for each firm. One agency publishes in its general reference book 1,300,000 firms and corporations. These are frequently changed by additions, obliterations, and other altered ratings; these data are impartial. Firms seek a rating upon going into business where their dealings are in distant markets. In this way the commercial world is dependent upon the agency.

The ratings for the general agencies are less

highly specialized than in the case of agencies covering special lines of business. For instance, the general agencies have about twenty signs for financial responsibility, and nine symbols for credit standings. On the other hand, the special agencies employ about twenty signs for capital ratings, and from eighty-five to one hundred for credit ratings. Full and accurate information is sought by the credit man, and in his view a valuable rating is one which aids in assigning the firm to a class, and indicates reasons for the assignment; to do this, however, is quite complicated and difficult.

The cost of the general agency service is $100 per year. This includes two reference books published every six months for the United States and Canada, with the privilege of one hundred special reports. In addition to these, the subscriber is entitled to weekly reports. The special reports cover the entire history of a firm, and include letters from other firms doing business with it.

The trades are classified, and the reporters work on specific lines, and by reason of the enormous amount of details covered and classified, no general merchant or banking firm could safely transact business without the aid of this service. It is done in the interests of those who must extend credit to distant firms. It therefore becomes quite obvious that the mercantile house

and the bank find here an indispensable fund of information in regard to the financial standing of all persons and firms asking credit.

But this is not sufficient. Each firm doing any considerable business must have its own credit department. The organization of this department is quite similar to that of the other departments of the business. Its existence becomes necessary in order that each order may be passed upon before it finally goes upon the books in the form of credit. The manager must have his own classified data in addition to that furnished by the general or special agency and credit clearing-house. The credit manager has oversight over the office force, bookkeeping, records, etc. In some firms he is, in fact, the manager, and has charge of the collections.

The credit information of a given firm is necessarily specialized along the line of its business. For this reason is must supplement the work of the general and special agency. The information must be well classified and accurate. It must be available for consultation between the receipt of the order and shipment of the goods. The information of the commercial agency is the basis of the work of the credit department of the firm. Slipshod methods do not inspire a high regard on the part of credit men. If the bookkeeping of the firm is lax and indefinite, it works

untold harm to the business. The credit man must be fully acquainted with his collateral.

The following tests of a good credit man have been suggested from the employer's point of view. One test is to find the average annual losses of the firm through bad credits. Another is to measure the accounts by the average number of the day's sale contained in them. Still another is to find the average percentage of discounts based upon receipts. Naturally, the most successful credit man is one who has the fewest losses, and holds trade. A shrinkage in business does not necessarily reflect upon the credit man. But it is obvious that the manner in which credits are handled greatly affect the total value of business. For instance, severity and extreme conservatism will drive away business, while freedom of granting credit may bring loss. The credit man can quickly ruin a business. As a financial authority his judgment is final. He knows every customer of the house by name, reputation and financial standing. It is a grave matter to deny credit, because it means the loss of trade, so that the credit man must move slowly. A successful credit man is one who will approve the largest number of orders, and keep his loss to a low percentage. In addition to his knowledge as a business man, he should also have a working knowledge of commercial law and bookkeeping.

The qualities which make a good credit man

cannot be put into exact terms. The work that he performs is the most delicate in the whole range of business. It is delicate because it touches a man at his most sensitive point; it concerns his property, character, and financial ability. It is one thing to have a good record as a credit man for refusing orders, and another to have a low percentage of loss upon large sales. For this reason a comparison of sales and expenses is a good indication of the good management of the credit department. The credit man is the guardian of the treasury and assets of the firm. He can create financial ruin, or he can develop financial strength, or he can destroy business by assuming a dangerous risk.

Some firms adopt the policy of passing only a portion of their orders through the credit department. To this department are sent only doubtful orders. A large percentage of merchants discount their bills, and are considered good credit. This method saves considerable unnecessary work, but it also has its dangers. For this reason the general policy is to require the credit department to approve all orders before shipment.

Operating in close connection with the credit department is the selling organization. This close relationship is obvious for the reason that the credit department of a firm must rely to a considerable extent upon the reports of the traveling salesman. In fact, bad credits often begin

with the salesman. He should not force an order where credit is doubtful, or induce the merchant to buy beyond his ability to pay. Formerly it was the custom of the salesman to push his sales to the largest extent, but the methods of compensation, and the relationship of the traveling salesman to the firm are now such as to restrain the salesman in taking orders where it is fairly certain that the credit department will not approve them. Naturally, the salesman desires to sell goods; the credit man, on the other hand, desires him to sell goods that can be promptly paid for. In this sense the sales and credit departments are supplementary. The salesmen of the best houses are taught the basic principles of credit, and work with the credit department. The credit man comes to know the judgment of a salesman on matters that concern his department, but the credit policy must necessarily be determined by the credit manager. Prizes are often offered to the salesmen who have the least number of disputed accounts; in some instances prizes are offered for credit information.

In recent years the credit men of the country have been doing a great work in developing better methods of collecting and classifying data through their national and local associations. In these annual conferences they compare experiences. Working together for mutual assistance are local, State and national credit men's associations.

They are working to get rid of the dishonest and incompetent buyers by a discussion of credit methods and systems, and other matters pertaining to credit. In this way a more enlightened management of the department is secured. The credit man is coming to know the value of co-operation, and is beginning to appreciate a more accurate knowledge of the margin of profits and of the secret methods of his debtors, and the value of accurate cost-keeping. The national association of credit men has an enrollment of about 5,000, and reaches every important trade community in the United States. It has done much to advance credit conditions, and to develop a proper credit departmental organization.

There has recently been organized what is known as the credit clearing-house. This institution was developed for the purpose of giving the credit man the same kind of service rendered by the clearing-house in other lines of business. It is a common meeting-place for the comparison of notes on the credit standing of the different firms. Its success is based upon a full and mutual co-operation of those belonging to the association. It is an exchange of credit or ledger experiences, and forms a medium between the debtor and creditor, which leads to a fuller knowledge of trade conditions. It has a plan of checking off information derived from various

sources; in short, it is a comparison of the ledgers of different creditors.

These ledgers are brought together at a central bureau and classified for mutual service. It prevents fraudulent over-buying, and has great possibilities in creating and maintaining normal conditions. It encourages credits for the reason that a merchant does not care to go on the interchange files for arrears in payment of bills. The credit clearing-house, however, has its limitations, and is best adapted to a special line of business. A form of the credit clearing-house is found frequently among retail merchants. It is a common practise for local merchants to cooperate in ascertaining the financial standing of their customers; in this way they compare accounts, and issue "black-lists." This system has met with success in the local field, and does for the retailer what the larger credit clearing-house does for the large business interests.

Protection against loss is sought wherever possible in modern business. We have noted how the dealer of grain and cotton is protected against loss by buying futures and options on the Board of Trade. The owner protects his property against loss by fire, as well as his life against accident and death. In recent years the principle of insurance has been extended to credits.

Insurance is designed to distribute the burdens and losses among a large number of interests.

It is based upon the law of averages as applied to risks. Credit insurance is similar to fire and life insurance, for the extension of credit involves the chances of loss. The custom for the business man is to cover his risks against fire by insurance has suggested the extension of the principle to bad debts; the principle of expectancy is here extended to his accounts. Every account has a natural expectancy, and this then becomes insurable; the credit insurance firm simply endorses the credit.

The rates of insurance are based upon the average losses through poor credit, and can be figured out with as much certainty as in the case of loss by fire or by death. Commercial mortality is determined by known data, and is classified according to the different lines of risks. While this form of insurance is not in general use, it has, however, some features to recommend it. But obviously the stability and value of credit insurance goes back finally to the stability of the insurance company. The most general form of credit insurance is undertaken by bonding and trust companies. These cover the risks of contract, or official relationships. Whenever an individual or company engages to do a certain work, the law of business practise often requires a guarantee of good service or a faithful discharge of duties. This does not always assume the form of credit insurance, but very often takes the form

of a guarantee of a return of money, or the faithful fulfillment of a contract. Some of these transactions, however, are mercantile in their character, and consequently involve the principle of credit insurance.

We will now turn to an examination of some of the credit problems peculiar to retailing. The problems confronting the retailer in regard to credit are more difficult than those of the larger mercantile firms. In the first place, these concerns are covered carefully by the larger mercantile agencies. But in the case of the retailer many of his customers are often without visible assets. It therefore becomes a delicate problem to know whom to trust or when to deny credit. The retail merchant must have about the same knowledge of the reputation, salary, and paying power of his customers that a cashier of a bank must possess in the smaller communities. Very frequently he must depend upon his own information.

Very few retailers have an organized credit department. They more frequently rely upon their knowledge of the community and of the trading public. As a result, losses are frequent in the retail trade. This has driven many retail establishments to a cash basis. Obviously, the loss through bad credit is not the only argument in favor of a cash trade. The other argument is based upon the lower price made possible by the

saving of interests. Of course, the adoption of the cash policy will depend upon the general prosperity and thrift of the community. The customer very often must be educated to it. But in the end it is more satisfactory than the credit system.

In order, however, to safeguard against losses through poor credit, many schemes have been suggested. The most general practise is to organize co-operative credit associations. This means in essence a credit clearing-house for the local trade, which becomes the repository of the information concerning the customers in the community. It may only affect a particular line of stores. The difficulties are obvious, because of the large number of customers. Each individual must have a rating, and it is often exceedingly difficult to secure authentic information, and then a great majority of the community do not possess much tangible property, and their ability to pay depends largely upon their reputation.

In the large city stores where credit is extended, the customer is given a credit-slip, which is presented to the salesman, and, if the information is not full, it goes to the credit department for investigation. In the larger cities it is the practise to assign to customers a credit limit beyond which the salesman cannot go unless so directed by the credit department. Under these circumstances

the individual who desires to trade on credit secures a rating, and receives an identification card, which admits him to credit. This places the customer in the same position as the merchant who goes to Bradstreet and Dun for a rating. When the credit man of the wholesale house begins to inquire into the nature of the accounts carried by the retailer, some of the more important lessons of credit are forcibly brought to his attention. He learns to use the same careful methods of inquiry which are employed by the larger wholesale firms. Of course, he cannot go into these details with the same fullness and accuracy, but he can learn something of the standard of living, the salary, the tangible property, and general reputation of the customer, and in this way reduce his losses due to poor credits.

Various devices have been used to induce customers to pay cash, or to settle their accounts in reasonable time. One scheme in successful operation is known as the Purchasers' Cash Discount Association. The central idea of this plan is to induce all the buyers to pay cash by offering a discount on all cash purchases made by those who belong to the association. Where these co-operative credit associations are organized, they form a credit clearing-house. The association furnishes information to the merchant in much the same way as is done by the larger associations for the wholesalers. Ratings are given and particular

attention is paid to the black-list. In this way the merchants are protected against those who are not able to pay, or never expect to pay, but who at the same time buy generously. These associations are springing up in all the important cities, and are doing an excellent work in promoting the credit conditions of the community in which they operate.

From the foregoing account, it will appear that a great deal has been done to place credit information upon a safe and scientific basis. An examination of the vast amount of work done by the great mercantile agencies is an evidence of the growing interest in the work of curtailing losses which come from giving credit. As this data is more thoroughly collected, and more carefully analyzed, credit will have more and more a scientific value; it is gradually emerging from a period of guesswork. The importance of safe credit is appreciated by the fact that business does not require cash so much as safe methods in ascertaining credit valuations. Business firms are willing to extend credit when there is a reasonable assurance that the accounts will be settled within a specified period.

The safest basis for commercial credit is properly collected and classified data. Of course, it must not be assumed that all losses can be foreseen by the credit man. If this were true, credit would be upon a thoroughly scientific basis; but

there are so many forces at work in the business world which cannot be accurately foretold, but which are likely to lead to losses at unexpected times. In 1903 one of the large mercantile agencies compiled statistics showing the causes of failure. The more important of the many causes cited are incompetence, inexperience, and lack of capital; the latter two are the more important causes. Inexperience accounts for twenty per cent., and the lack of capital for thirty-two per cent. of the total number of failures. The next important cause of failure is through specific loss, such as fire, which could not, of course, be foretold by the credit man. It is estimated that fully eighty per cent. of all the failures can be diagnosed and foretold by the credit manager. If this is true, the data and information underlying the extension of credit is fairly well understood, and in view of the increased effort everywhere to become acquainted with the methods of collecting and ascertaining credit, as well as the principles of rating, it will result in the end in placing this phase of mercantile activity upon a sound basis.

Closely allied to the work of the credit department is that of collections. They are so intimately related that it is impossible to separate them in business. The aim of the credit department is to keep the accounts upon a collectable basis, and when this is done the work of the collection department obviously becomes simple.

In fact, the two services are so closely allied that they are frequently handled by the same organization.

The methods of making collections vary widely in practise. In some instances the collections are left to the credit department; but where the business is conducted on a large scale, the collections are turned over to a separate department. Most of the large firms have a collection manager, who works in connection with the legal and credit departments. It is obvious that consultation with the credit manager will indicate the standing of the customer, and where claims must be pushed, the legal department must be called in for advice and assistance. However, as in the case of credits, a number of agencies have grown up devoted to making collections. These agencies are both special and general. The special agency is one which takes up a particular line of collections, while the general agency covers most of the trades; an example of the special agency is found in the newspaper-collection agency.

The best illustration of the general agency is Bradstreet and Dun, who have added to their credit work a collection business. Another type of the special agency is the local company which takes the accounts of merchants for collections. In most instances collections are made upon a percentage basis. It frequently happens that the local retail associations do a collection business.

Another method frequently employed by wholesale houses and manufacturing firms is to permit their salesmen to make collections. In some instances the salesmen are made responsible for their sales, and must turn into the firm's treasury the full amount of sales, upon which they receive back a certain percentage. The failure to do so is a loss charged against the salesman. This form of collection is very frequently employed by laundry firms. They find it more economic to give a laundry agent certain territory, charge him at the laundry for the work brought in, and in this way make him personally responsible for the collections.

But the functions of selling and collecting are entirely distinct, and call for special talents in each direction. A man may be a good salesman and yet be a poor collector. A salesman is by nature an optimist, but the collector must have sterner qualities. Again, collections interfere with the work of the salesman. There is always a competition for the trade of the slow-paying customer. The customer naturally lodges his complaint against the collection department, and if the salesman makes collections, it naturally tends to drive the customer from him.

We may now turn to the consideration of the methods employed in making collections. The great bulk of outstanding accounts and credits is essentially self-collectable. In other words,

the debtor consents voluntarily to pay. The credit is usually extended for a definite period, usually from thirty to sixty days. Often an open account is carried, with the understanding that remittances will be made at stated intervals. These are voluntary payments, and the machinery for collection is only nominally called into operation.

Another method of securing prompt payment is through the system of discounts. By offering a discount, if payment is made within a stated time, many accounts are settled without a resort to sterner methods. By sending out letters at certain intervals, the attention of the creditor is called to slow payments, and accounts are gradually settled. It is frequently understood between the creditor and customer that at certain intervals the firm is free to draw upon the debtor. This is quite frequently done in business. We do not refer to those drafts sent to banks for collection, but rather to those which are sent according to an understanding.

In addition to these voluntary payments, are a number of methods employed to bring about forced payments. One of the most usual methods is through the collection upon C. O. D. shipments. In one sense this cannot be considered as a collection of an outstanding credit, but the method is used to prevent a bad credit, and is a safeguard quite generally employed in business.

In certain lines of business the C. O. D. shipment is frequently made, and where the firm does not care to extend credit, it is effective in the end to adopt this policy in extreme cases.

Another phase of forced collection is through a draft sent to a bank or agency for collection. This calls into operation the organized machinery designed for this work. These collections are those which have proven fruitless by simpler methods.

Finally, if the above methods fail, legal procedure is resorted to. Frequently, before this is done, the merchant may be permitted to give a note, which may now be sold, thus shifting the collection to another party; but if these methods fail, prosecutions are begun to force payment. Sometimes suits are pressed in order to get judgment, which may be enforced at such time as the debtor can meet his obligations.

It is thus seen that the great majority of accounts are settled upon the presentation of a statement at frequent intervals, whereby the attention of the customer or debtor is called to the statement of his account. Only a small percentage of accounts are subject to forced payment, but yet in their sum total they are sufficiently large to call into activity a considerable number of persons whose business it is to make collections. Still, however, as the proverb reads, "an ounce of prevention is worth a pound of

cure;" the question of collections finally goes back to the problem of credits. Yet, in spite of the alertness of the credit department, nevertheless some loss must be expected through credit risks. The credit department cannot conduct the business upon an absolutely safe basis, but must take some risks in order to enlarge and hold its trade. But in view of the fact that it is the business of the credit department to keep its accounts upon a collectable basis, it might naturally be assumed that in time the mercantile business will be fairly free from losses of this character.

It is scarcely necessary to refer to the legal phases of credits and collections. Naturally, the law has amply protected the creditor against fraud, and has imposed severe penalties upon those who incur obligations beyond their ability to pay. In addition to the rules of law generally recognized as bearing upon this subject, legislatures have greatly strengthened the position of the creditor. Especially is this the case with the treatment of accounts and bankruptcy. Legal protection alone operates as a wholesome check in business.

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